UPdate

LINKING ASSETS INC.

A Jaisan Recovery Corp.

MARCH 2019

LINKING ASSETS INC.

A Jaisan Recovery Corp.

In this UPdate

Linking Assets Inc. UPdate periodically provides articles and information regarding legislative, regulatory, compliance, and associated developments. Keeping you informed about unclaimed property, search and location, owner outreach, and related areas of interest.

Unclaimed Property Dos and Don'ts

By Christa DeOliveira, CIA, CCEP

Just like in many other areas of our lives, there are dos and don'ts when it comes to unclaimed property. Although, with unclaimed property, missteps can potentially have financial and resource impacts.

Do: Always perform owner outreach/due diligence before reporting and remitting unclaimed property. Ticking off this important requirement can help reunite owners with their property and avoid the need to remit it to the respective state.

Additionally, some states have specific penalties for not performing outreach, potentially ranging from report rejection (with interest accruing) to penalties. Va. Code Ann. §55-210.26:1 (B) specifies "Any person who does not exercise due diligence… shall pay a civil penalty not to exceed fifty dollars for each account upon which due diligence was not performed." Consequently, for Virginia a holder could be fined up to $50 for each incidence of not sending a required due diligence letter.

Finding updated addresses increases success rates. Several states require looking for new addresses, for example, according to Fla. Stat. § 717.101(9)

> "Due diligence" means the use of reasonable and prudent methods under particular circumstances to locate apparent owners of inactive accounts using the taxpayer identification number or social security number, if known, which may include, but are not limited to, using a nationwide database, cross-indexing with other records of the holder, mailing to the last known address unless the last known address is known to be inaccurate, or engaging a licensed agency or company capable of conducting such search and providing updated addresses.

Be sure to include foreign addresses in your due diligence mailings. In the securities arena there have been some cases where due diligence has not been sent to foreign addresses, with costly results. In the case *Azure Limited v. I-Flow Corporation*,[1] the California Supreme Court ruled statutory immunity for holders who report and remit funds are limited to situations where the holder complies with other provisions of the

[1] *Azure Limited v. I-Flow Corporation*, Cal. (2012)

unclaimed property law including due diligence/owner notification provisions. In conjunction with this case California changed its statute to include similar language. Cal Code Civ Proc § 1560(a) instructs holders will be relieved from liability if the holder has

> [H]as made reasonable efforts to notify the owner by mail or, if the owner has consented to electronic notice, electronically, in substantial compliance with Sections 1513.5, 1514, 1516, and 1520, that the owner's property, deposit, account, shares, or other interest will escheat to the state, is relieved of all liability to the extent of the value of the property so paid or delivered for any claim which then exists or which thereafter may arise or be made in respect to the property.

Do: Communicate early and often with property owners. Holders need not wait until the required due diligence window to communicate. Sending out notices or contacting owners in advance of the required deadline elicits more responses and reunites more owners with their property.

Do: Report on time with the correct format, with property details in the correct fields. Variations of reporting formats are required by states. Mainly the requirements are based on the NAUPA 2 format. As with variations in state laws, there can be differences for reporting too. Generally, the fixed width fields are designated to contain specified information in a required format, such as alphanumeric for street addresses or formatted as dates for last activity dates.

Getting data elements into the correct field reduces the need for data scrubbing, reduces the likelihood for a report to be rejected, and increases the ability for states to return property to the correct individual(s). Better information should also lead to less follow up inquiries from states.

Getting data into the appropriate field can also protect holders; if an owner's social security number was inadvertently placed in an incorrect field on the report and it was subsequently posted on a state's website, it would be a privacy breach. Data in the correct fields avoids this altogether.

NAUPA is developing a new format, NAUPA 3. This will do away with the outmoded fixed width field format. It is being programmed leveraging Extensible Markup Language, commonly referred to as XML; paving the way for more logical and detailed reporting. The new format is being worked on and specific rollout dates are unknown.

Don't: Claim property in a state's custody before reporting to that state. If state personnel were to compare a listing of companies that report to their state to a list of companies claim from them, how would you stack up? Some states do make this comparison and depending on a holder's compliance level, this could elicit unwelcome enforcement attention.

Don't: Miss reporting of common property types for your industry. There are patterns of reporting related to the industry or industries your company is in. Ensure all the common property types for your particular industry are being captured and reported. To learn more, join industry groups and associations, increase internal research and education, hire experts, or pursue a combination of these approaches.

Don't: Think you are done once you have submitted an unclaimed property report. Along with the ongoing and future compliance reporting activities, keep excellent historical records for each reporting cycle for at least 10 years plus the longest dormancy period on the report. Including, but not limited to, the reports, supporting documentation; documentation of the reasoning for any property deemed to not be eligible for reporting; and keep proof of remittances, such as cancelled checks, wire transfer, and ACH debit/credit. Essentially, if it has a bearing on what was reported, remitted, and transferred, then keep it.

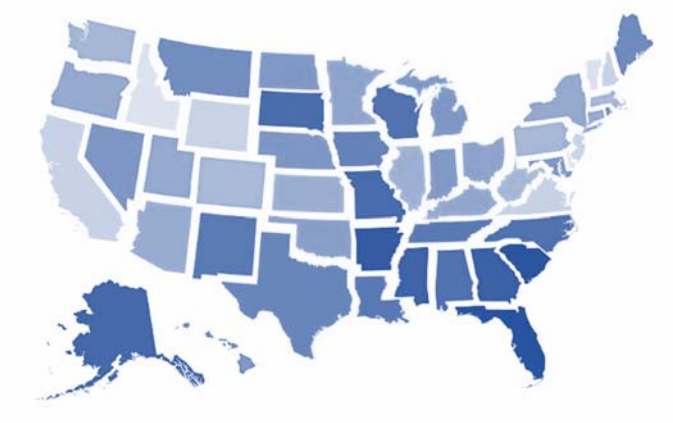
Having complete and accurate records is only as good as they are accessible. As ongoing business systems are changed, keep in mind that historical records could need to be accessed, viewed, searched, and researched. Incorporating these abilities into the scope of system change projects will result in mitigating some of the risks associated with enforcement actions, such as decreasing estimations because actual records can be relied on.

With another cycle of unclaimed property compliance reporting always around the corner, holder unclaimed property programs can always benefit from good dos and don'ts practices.

Legislation Updates

Linking Assets Inc. monitors the progress of legislation effecting unclaimed property related topics. Being early in the year, many state legislatures are in session, and considering bills related to unclaimed property. Highlights of enacted and noteworthy pending legislation are provided here.

Linking Assets Inc. is not a law firm and does not render legal services or advice. The information in this UPdate is not intended to be substituted for legal advice, which can only be provided by an attorney.



Enacted Legislation

AR HB 1427 effective upon enactment, March 15, 2019
This legislation allows, but does not require, for the immediate liquidation of securities. Claimants may receive the securities if they remain in the custody of the administrator, or alternately they may receive the proceeds received from liquidation, less any fees and expenses incurred by the sale.

NE LB 406 effective upon enactment, March 12, 2019
This bill changes various provisions relating to unclaimed property reports and notices, disposition and transfer of funds, and duties of the state treasurer: including raising the state's notice publication threshold from less than $25 to less than $50.

TN SB 240 effective upon enactment, March 13, 2019
This bill adds transit fare cards as property not included in the definition of property of unclaimed property.

WY HB 29 effective 07/01/19
Exempts interest accrued on life insurance policies or retained asset accounts from unclaimed property. Also, imposes requirements for providers of life insurance, annuity contracts, and retained asset accounts to confirm death of insureds/account owners. Allows for penalties for non-compliance.

Pending Legislation to Watch

There are several state legislatures where bills have been introduced to enact a state-specific version of the Uniform Law Commission's *2016 Revised Uniform Unclaimed Property Act.* These include:

- CO SB 88
- MN HF 2208, SF 2611
- NV SB 44
- SC HB 4200, SC SB 524
- WA HB 1179

Compliance, Regulatory, and Legal News

GAO recommends: The Government Accountability Office reviewed transfers of retirement savings accounts, such as a 401(k)s and IRAs, to state unclaimed property divisions. While the report acknowledges there is some guidance from both the IRS and the Department of Labor, yet the IRS has not clarified the tax reporting and withholding requirements for employers making these transfers of unclaimed retirement funds. Federal law seeks to protect the interests of retirement plan participants. Therefore, the GAO has made three specific recommendations:[2]

1. The IRS Commissioner should work with the Department of the Treasury to consider clarifying if transfers of unclaimed savings from employer-based plans (such as 401(k) plans) to states are distributions, what, if any, tax reporting and withholding requirements apply, and when they apply.
2. The IRS Commissioner should work with the Department of the Treasury to consider adding retirement savings transferred to states from

[2] https://www.gao.gov/products/GAO-19-88

terminating DC plans to the list of permitted reasons for rolling over savings after the 60-day rollover period, in a form consistent with the rules adopted on the taxation of transfers of unclaimed retirement savings.

3. The Secretary of Labor should specify the circumstances, if any, under which uncashed distribution checks from active plans can be transferred to the states.

The full GAO report, entitled *Retirement Accounts: Federal Action Needed to Clarify Tax Treatment of Unclaimed 401(k) Plan Savings Transferred to States* can be viewed online.[3]

Goldberg v. Frerichs: on January 2, 2019, the U.S. Seventh Circuit Court of Appeals decided "the Takings Clause of the Constitution protects the time value of money as much as it does the money itself."[4] Whether a claimant is entitled to the time value of money is not dependent on what the property had been earning prior to being reported and remitted to state. The decision notes charging a bookkeeping fee is allowable and for small accounts. Ultimately, this fee might exceed the property's time value, but the state must allow the benefit of the owner's property's earnings, regardless of how large or small they end up being.[5]

The decision also gives an example of a coin stored in a safe deposit box which is turned over to the state for nonpayment of the rental fee. Noting that, even though the coin was not earning interest while it was in the safe deposit box; it was an investment property where the owner hoped that its market price would increase. Subsequently, if the state had kept the coin and returned it based on an owner's claim, then interest would not be owed. The owner could then sell the coin and get any change in value that occurred while it was in the state's custody. However, if the state liquidates the coin, it cuts off the possibility of appreciation. The circumstance that the coin was not previously "earning interest in the safe deposit box would not detract from the fact that its price could rise. The loss of that time value is compensated by giving Owner the benefit of interim earnings."[6, 7]

The circuit court vacated the district court judgement, and the case was remanded for proceedings consistent with cited case law and the findings in the opinion.

Illinois Administrative Rules- The hearing on October 18, 2018, and comment period related to the proposed Administrative Rules resulted in extensive feedback and requests for changes. The Illinois State Treasurer's Office has responded directly to the entities and individuals that provided comments and intend to proceed with the rulemaking process.

Timbs v. Indiana- The Supreme Court issued a unanimous decision on February 20, 2019, in this case dealing with excessive civil penalties.[8] If holders find themselves being subjected to excessive civil penalties this case can be relied on to address this. As noted in *Timbs*, the implications increase when the penalties are assessed for the purpose of raising non-tax revenue.

The court concluded the case for Fourteenth Amendment incorporating the Excessive Fines Clause is overwhelming and has both a historical and logical basis. the Excessive Fines Clause provides protection "against excessive punitive economic sanctions secured by the Clause"[9] and is both "fundamental to our scheme of ordered liberty" and "deeply rooted in this Nation's history and tradition."[10]

As a matter of background, Tyson Timbs did plead guilty in Indiana state court to both, dealing in a controlled substance and conspiracy to commit theft. He was sentenced to a year of home detention and five years of probation. The probation included a court-supervised drug treatment program. He was required to pay fees and costs totaling $1,203. When Timbs was arrested, the police seized his Land Rover. Incidentally,

[3] https://www.gao.gov/assets/700/696525.pdf
[4] *Goldberg v. Frerichs*, 912 F.3d 1009, U.S. App. (2019)
[5] Ibid
[6] Ibid
[7] The example of an investment could relate to other forms of investment, such as securities and mutual fund shares.
[8] *Timbs v. Indiana*, 586 U.S. ___ (2019)
[9] *Timbs* quoting *McDonald v. Chicago*, 561 U.S. 742, 767 (2010)
[10] Ibid

Timbs had purchased the SUV for about $42,000 using life insurance proceeds from his father's death.

Subsequently, using a private law firm, the state brought a civil suit for forfeiture of Timbs's SUV, based on the vehicle having been used to transport heroin. Although finding that Timbs's vehicle had been used in his crimes, the trial court denied the request for forfeiture. This was based on the purchase price of the vehicle was over $42,000, which is more than four times the maximum $10,000 fine which could be assessed for his drug conviction. The lower court determined forfeiture would be grossly disproportionate to Timbs's offense; thereby being unconstitutional under the Eighth Amendment's Excessive Fines Clause.

Later, the Court of Appeals of Indiana affirmed the determination, while the Indiana Supreme Court reversed it. The Indiana Supreme Court held that the Excessive Fines Clause is inapplicable to state impositions and only constrains federal action. However, the Indiana Supreme Court did not decide if the forfeiture would be deemed excessive.

The Excessive Fines Clause's venerable heritage can be traced as far back to the Magna Carta, if not longer. The Magna Carta prescribed for economic sanctions to "be proportioned to the wrong." Later, on this side of the pond, almost verbatim language was adopted, first in the Virginia Declaration of Rights, then in the Eighth Amendment. Adoption of the Excessive Fines Clause was in step with English law and it resonated with similar colonial-era provisions, for good reason, the protection against excessive fines has been a constant shield throughout Anglo-American history. Today, all 50 States have a constitutional provision prohibiting the imposition of excessive fines either directly or by requiring proportionality.[11]

Even absent other motives, the decision notes fines may be used "in a measure out of accord with the penal goals of retribution and deterrence," for "fines are a source of revenue," while other forms of punishment "cost a State money."[12] Further, it is raised that fines are used as a source of revenue "because they are politically easier to impose than generally applicable taxes, state and local governments nationwide increasingly depend heavily on fines and fees as a source of general revenue."[13]

Justices Gorsuch and Thomas concurred. In Justice Gorsuch's concurrence he stated that the Fourteenth Amendment makes the Eighth Amendment's excessive fines prohibition fully applicable to States. However, he adds he does not agree with the route the Court took to reach this conclusion. He asserts that instead of interpreting the Due Process Clause to incorporate a "substantive right that has nothing to do with "process," I would hold that the right to be free from excessive fines is one of the "privileges or immunities of citizens of the United States" protected by the Fourteenth Amendment."[14]

Recalling an unclaimed property case which appeared to have excessive fines, the court documents of *Temple Inland*[15] state $147.30 of unreported unclaimed property was found to be escheatable to Delaware in the identified base years of the audit. Although, the assessment was for $1,388,573.97. This illustrates the unclaimed property implications of *Timbs.* Also as noted in *Timbs*, the implications are stronger when the penalties are assessed to raise non-tax revenue.

[11] *Timbs v. Indiana*, 586 U.S. ___ (2019)
[12] Ibid
[13] *Timbs,* quoting Brief of the American Civil Liberties Union, The R Street Institute, and the Southern Poverty Law Center as *Amici Curiae* in Support of Petitioners

[14] *Timbs v. Indiana*, 586 U.S. ___ (2019)
[15] *Temple-Inland, Inc. v. Cook,* 192 F. Supp. 3d 527 (2016) U.S. Dist. Del.

Contact Us

535 5th Avenue, 26th Floor
New York, New York 10017
(212) 256-1155 | www.linkingassets.com

PETER QUINN, CPA
Chief Executive Officer, Co-founder
peter.quinn@linkingassets.com
(914) 498-5600

RUDY QUINN
President, Co-founder
rudy.quinn@linkingassets.com
(914) 498-8600

RICHARD J. AMODEO
Co-founder
rich.amodeo@linkingassets.com
(917) 363-8040

CHRISTA DEOLIVEIRA, CIA, CCEP
Chief Compliance Officer, Editor
christa.deoliveira@linkingassets.com
(801) 641-4054