

Be On Alert - State of Delaware Ramps Up Unclaimed Property Enforcement

Client Alert

03.11.2019

For those who thought the State of Delaware had gone out of the unclaimed property business - think again. After a 2017 overhaul of Delaware's unclaimed property laws and an increased emphasis on voluntary compliance with those laws, Delaware is sending out dozens of "invitations" to companies to enter its Abandoned or Unclaimed Property Voluntary Disclosure Agreement Program (the "VDA Program"). Ignoring this invitation guarantees that a company will get audited by the state. Delaware is also beginning to review companies' reporting histories and their annual unclaimed property filings for accuracy and completeness and is strictly enforcing timelines and deadlines for companies under audit. All of this is a signal to Delaware companies that, while voluntary compliance is preferred by the state, audit - with assessed interest and penalties - is a very real consequence and an alternative that Delaware can and will pursue.

UPTICK IN DELAWARE UNCLAIMED PROPERTY AUDITS AND VOLUNTARY DISCLOSURE INVITATIONS

In December of 2018 and February of 2019, the State of Delaware sent dozens of letters to companies organized under the laws of the State of Delaware indicating that those companies are likely out of compliance with Delaware unclaimed property laws and inviting such companies to participate in the Delaware Secretary of State's VDA Program. The State Escheator has confirmed that, if a company does not elect to participate in the VDA Program within sixty (60) days following the date of such letter, it will for a fact be audited. These letters are typically sent to the Chief Financial Officer of a company with a copy (per the State's more recent practices) to the registered agent and may appear relatively innocuous and, therefore, are often ignored. However, it is critical that a company recognize this letter when it receives it, so that it has the ability to make a deliberate determination regarding participation in the VDA Program.

There are a number of key factors that a company should consider in making a determination of whether to participate in the VDA Program or be subject to an audit, which would require a comprehensive discussion with counsel that specializes in this area. However, a few of the more significant points to consider are as follows:

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1. interest for certain and perhaps penalties will be assessed in a Delaware audit, but all interest and penalties are waived under the VDA Program;
2. an audit involves a third-party contract auditor often compensated under a contingent fee arrangement where their pay could be tied to the size of the state's recovery whereas the VDA Program involves a self-review, typically with the assistance of outside counsel and/or consultants, although the state does employ third-parties to help administer the VDA Program;
3. audits often last 3 to 6 or more years with other states joining the audit while VDAs do not involve other states and usually last 2 years or less; and
4. the Delaware audit program is administered through the Division of Revenue while the VDA Program is administered through the more "business-friendly" Secretary of State.

There are a number of other factors that should be considered, so the right decision will be based on the specific facts and circumstances for a particular company.

INITIATION OF COMPLIANCE REVIEWS BY THE STATE ESCHEATOR

Further, companies need to know that Delaware is focusing on annual unclaimed property filings made by companies and on ensuring that such annual filings are not inaccurate, incomplete or fraudulent - and this could include companies that have previously been audited or completed VDAs with Delaware. If the State Escheator believes that a report is inaccurate, incomplete or fraudulent, it has a statutory basis to authorize a "compliance review." Based on our discussions with Delaware's Office of Unclaimed Property, as well our own experience with our holder clients, a pilot program for compliance review has been initiated. For holders who have previously filed but did not file this past year, the State Escheator may be sending such companies a letter requesting copies of such companies' unclaimed property policies and procedures as well as a verified report (wherein a company representative must provide an affidavit that the company has no unclaimed property to report). The State Escheator's compliance review program is not a traditional audit but can result in a finding of liability or could result in an audit, depending on the nature and scope of a company's perceived reporting deficiencies, by property category, year or other relevant factors.

STRICT ENFORCEMENT OF THE TWO YEAR DEADLINE IN EXPEDITED AUDITS

Finally, in 2017 Delaware passed legislation allowing holders then under an unclaimed property audit by the state to either convert their audit into a VDA or enroll in an expedited audit. For those who chose the expedited audit route, the law makes clear that they must complete the audit on an expedited timeline of no more than two years which ends on December 11, 2019. The state's auditors have only an 18-month window within which to request records, testimony and other information and holders are expected to respond fairly and promptly to request and, if found to have not done

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so, risk removal from the expedited audit program, reinstatement of a conventional audit and assessment of interest and penalties by the state - something the holder avoided in the first instance by entering the expedited audit. With December 11, 2019 about 9 months away, Delaware has started sending pointed letters to certain holders in expedited audits, criticizing holder unresponsiveness to outstanding requests and attempting thereby to either get requested information or create the record which would support holder removal from the expedited audit programs and the ensuing guarantee of assessed interest and possible penalties. Holders must be on alert, must not ignore these letters and must object in writing to vague or overreaching auditor requests in order to protect holder interests - and the record - in these audits, where ejection from the program will involve significant additional interest and possible penalties by Delaware.

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PRACTICE AREAS

Unclaimed Property

