

UNCLAIMED PROPERTY – MAYBE A LITTLE SPRING CLEANING IS NEEDED

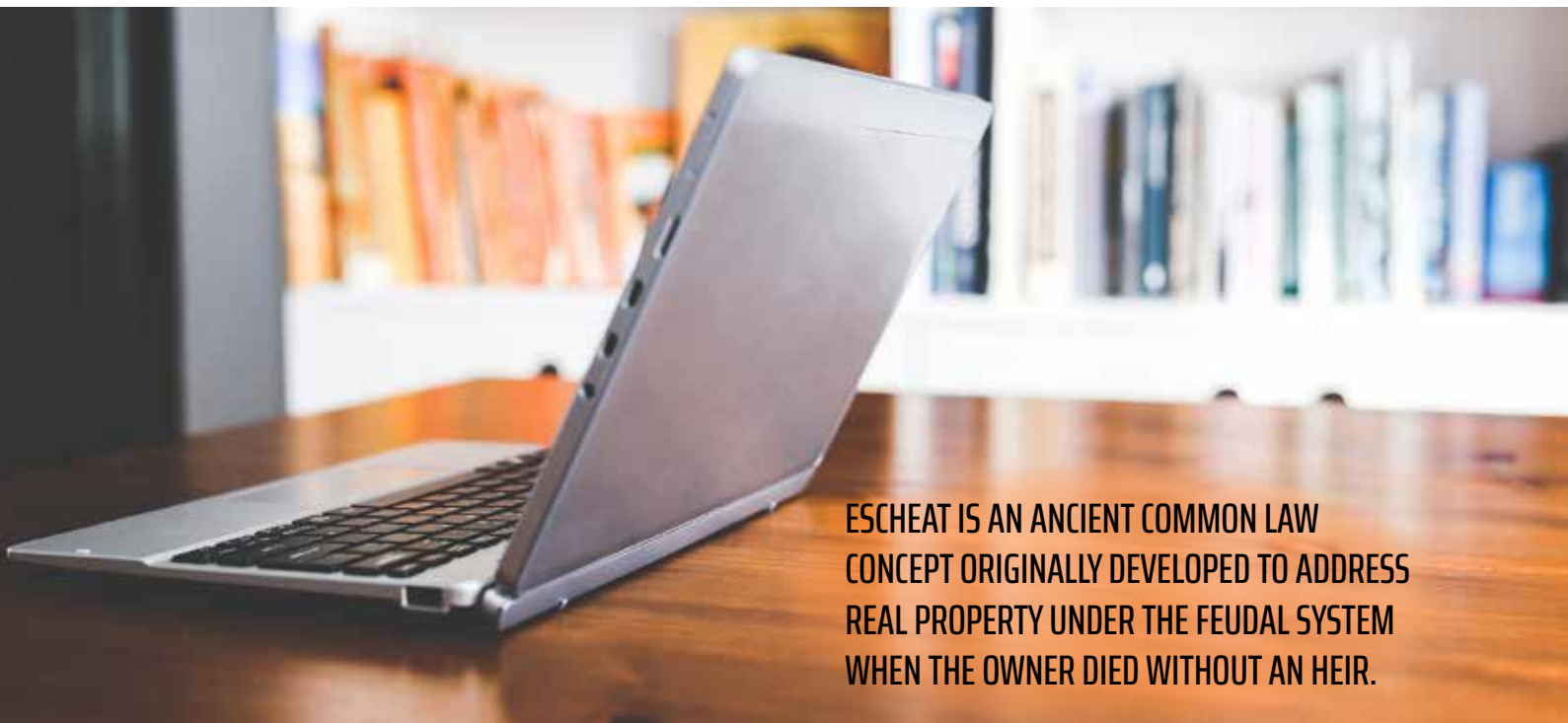
By Don Carpenter, MSAcc/CPA

When reviewing the accounts receivable subledger, have you noticed the odd lingering credit balance from the customer who overpaid or returned goods that just cannot get cleared because the customer can no longer be located? Or what about the payable balance where all efforts to pay the vendor have met with no success? These balances may not be material, but may require explanations in an analysis of the accounts. The organization may even have a policy of clearing those balances periodically to clean up the financial statements.

These lingering balances, although immaterial, belong to someone (possibly a customer, employee or supplier) and fall under the escheat rules that govern unclaimed property. Escheat is an ancient common law concept originally developed to address real property under the feudal system when the owner died without an heir. The property then went to the Crown in an effort to prevent land from becoming unproductive due to lack of ownership.

The concept has evolved to encompass all unclaimed property, including financial and even intangible assets. Management of unclaimed assets is regulated and enforced by the various states. Unclaimed property must be delivered to the state and becomes the property of the state until such time as its rightful owner claims the item.

What is the responsibility of the holder of unclaimed property? That depends on the state that governs the particular unclaimed asset, which is generally determined by the last known address of the rightful owner. If the owner's address is in Texas, then Texas law governs compliance. But if the last known address is in California, California law governs even though the holder of the property may be operating from a Texas establishment. In today's age of internet commerce, it is almost a requirement that most companies be familiar with the unclaimed property laws of all states or have access to a service provider who can provide such information.



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Using Texas rules as an example, the holder must first determine that the item qualifies as unclaimed property. For an unclaimed paycheck or utility deposit, the abandonment period is one year. But for financial assets, such as a bank account or safe deposit box, the period is much longer at five years. Most property, such as customer receivables or supplier payables, require a three-year dormancy period.

Once qualified as unclaimed property, the holder must send a letter to the last known address of the owner if the balance is greater than \$250. If no response is forthcoming, the holder of the property must provide a report to the Texas Comptroller listing all unclaimed property (even balances less than the \$250 notification threshold) and then shortly thereafter transfer ownership of the property to the state. Transfer of most unclaimed property is generally as simple as cutting a check for the balance of accounts. But in the case of tangible property, such as the contents of a safe deposit box, transfer of the tangible property is required. Each state will have its specific dormancy periods and procedures for relinquishing property.

One last complicating factor concerns determining which state has a claim on the property when there is no address for the rightful owner. The U.S. Supreme Court established priority rules in *Texas v. New Jersey* in 1965. After the priority given to the state of the owner, second priority is given to the state of domicile of the holder. For corporations, the domicile is the state of incorporation. For unincorporated entities, domicile may be defined as the principal place of business or place of formation.

Delaware has been quite active in enforcing unclaimed property regulations given the high number of entities that are incorporated within the state and the likelihood that the second priority rule applies. Following Delaware's lead, other states have responded with audits of businesses

that have a prominent presence within the state. The enforcement efforts of the various states have streamlined to multistate unclaimed property audits outsourced to third party specialists. Non-compliant businesses are subject to interest and penalties on any retained property and there is no statute of limitation restricting the years states may audit.

Many states have implemented voluntary disclosure programs that waive or reduce interest and penalties to encourage businesses to become compliant. Voluntary disclosure requires that a business continue to be compliant going forward. Disclosure requirements have received increased emphasis, as revenue sources in some states have declined and fiscal budgets have become tighter over the past few years.

Most states maintain websites with a list of unclaimed property that has been relinquished by holders. There is generally no statute of limitations for rightful owners to reclaim the property from the state. Several enterprises that specialize in locating owners and notifying them of possible claims in exchange for a commission upon successful reimbursement by the state have emerged over the past few years.

In addition to being compliant as a holder of unclaimed property, businesses should consider periodically reviewing state websites for possible claims. Given the complexity that arises from business acquisitions and combinations, successors in interest may find that material reimbursements are available.

Managers may be well advised to review accounts receivable and accounts payable for possible unclaimed property balances and become familiar with the procedures that govern administration of these funds. ■



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