New (but not necessarily good) Innovations and Best Practices

Changes in Unclaimed Property requirements

Fast Facts & Basic Background

- Origins in British Common Law
- Escheat
  - Traditional
  - Custodial

*Definition: Intangible personal property that has gone unclaimed by the rightful owner after a specified period of time

State and Federal Rules

- 54 jurisdictions have unclaimed property laws
  - Some states have adopted versions of the Uniform Unclaimed Property Acts while others have not; laws are constantly changing
- Supreme Court Case Law – priority rules for reporting
  - Texas v. New Jersey (1965)
  - Pennsylvania v. New York (1972)
  - Delaware v. New York (1993)
- Uniform Unclaimed Property Acts
  - 1954 Uniform Act
  - 1966 Uniform Act
  - ***1981 Uniform Act –specific language regarding Life Insurance***
  - 1995 Uniform Act
  - ULC currently revising the Uniform Unclaimed Property Act

Holder Responsibilities Under the Unclaimed Property Laws

- Duty to file a report timely
- Duty to perform due diligence timely
- Duty to remit the property timely
- Duty to maintain copies of the reports and supporting documentation
- Duty to protect the funds until reported and transferred to the state
- ***Additional rules unique to insurance***

Examples: Asset Types

- Benefit payments
- Accounts Receivable
- Accounts Payable
- Commissions/Comp
- Uncashed checks
- Gift Cards
- Unidentified deposits
- Refunds/Rebates
- Unapplied payments
- Business-to-Business
- Unpaid dividends
- Retirement Assets
- Customer credits
- Travelers' checks
- Matured bonds
- Securities shares
- Dormant Accounts
- Workers' Comp
- Other G/L items
- Tangible property

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Dormancy

Property is "presumed abandoned" 3-5 years after:

- Lost Owner
  - RPO Mail (returned as undeliverable)
  - Invalid Addresses
- Obligation to Pay
  - Dividend distribution
  - IRA Required Distribution Dates
  - Insurance proceeds
- Inactivity
  - Uncashed Checks
  - No "owner-directed" activity
- Death
  - Passive vs Active review
  - Social Security Administration "Death Master File" comparisons
  - Transfer on Death/Beneficiary Provisions

Where to Report

1. State of owner's last known address

2. State of holder's incorporation or domicile if address not known

3. State of holder's incorporation or domicile if address of apparent holder is in a foreign country <u>and</u> if holder is incorporated or domiciled in the U.S.

Fines, Penalties and Interest

- A holder can be assessed penalties and/or interest for:
  - Failure to report/remit the property
  - Failure to comply with the statute
- Interest generally applied at 10%-25% of property value
- Civil/Criminal penalties for failure to report/remit/deliver
- OR filing a fraudulent report may include:
  - $100-$200 per day ($10,000 maximum)
  - Varies from $1,000-$25,000 fine plus some states access an additional 25% of the value of the property
  - Some states – Class B misdemeanor

* ***Other fines and penalties related to insurance regulations may also apply***

State Unclaimed Property Laws vs. Federal Laws

Sarbanes-Oxley

- Failure to properly account for an unclaimed property liability (FASB Statement No. 5) could be in violation of Generally Accepted Accounting Principles (GAAP)
- Sarbanes-Oxley Act
  - Section 302 requires that CEOs and CFOs include, with any periodic financial report filed at the SEC, a written statement certifying disclosure controls and procedures.
  - Internal control is a significant focus of Sarbanes-Oxley due to recent financial and accounting scandals
  - Section 404 review includes an assessment of the design and operating effectiveness of internal controls for significant accounts
  - Compliance by SEC registrants is non-negotiable

ERISA

Various case law – in most cases the state's have agreed that ERISA federally pre-empts state unclaimed property laws

Internal Controls & Areas of Risk

- Until the property is transferred, ensure that adequate internal controls are in place and operating effectively!
- Consider establishing an unclaimed property liability account on the company's G/L if one is not already in place.
- Set up specific procedures for claims processing to incorporate the identification of unclaimed property.
- Set up specific procedures for due diligence and reporting timeframes and responsibilities or consider outsourcing.
- **Whistle-blower laws!**

When/Where to involve Legal

- Preventative
  - Review of Policies/Procedures
    - sufficiency with the legal requirements
    - consistency with legal requirements
  - Evaluation of Organizational readiness for audit
    - Proper identification and tracking of UP
    - Proper record keeping and record retention
    - Proper reporting
    - Identify/Resolve gaps
  - Voluntary Disclosure Agreements

When/Where to involve Legal

- Defensive
  - Receipt of Audit Notice
  - Non-Disclosure Agreement Negotiations
  - Audit Methodology/Parameters
    - Audit records back to 1981 (35 years)
    - Estimation/Extrapolation for lack of records
  - Audit Data Demands
    - "We're in compliance. We have nothing to fear. Let's just provide what they request."
  - Data Management
    - Similar to complex litigation discovery and data management.

When/Where to involve Legal

- Challenging the Audit
  - Scope of Audit
  - Dormancy Triggers
  - Appropriate Data – Constitutional Limits
  - Audit Findings – Evaluation & Negotiations
  - Closing/Settlement Negotiations

Suggested Best Practices

- Centralization over the governance of policies and procedures
  - Compliance Department
  - Internal Audit Department
  - Individual Life & Annuity Departments
  - Claims Department
  - Finance Department
  - IT Department
  - Unclaimed Property Department
- Preparation for an unclaimed property audit
  - Unclaimed property policies and procedures
  - Insurance industry high-risk areas of audit focus

Suggested Best Practices

- Laws
  - Am I holding unclaimed property beyond the dormancy period?
  - Am I following best practices and demonstrating valued customer expectations
- Accounting issues: Contingent liabilities, the snowball effect you want to avoid
- TPA agreements
  - Define responsibility for reporting unclaimed property
- How to be proactive and not reactive in identifying property to be escheated
  - Establish an unclaimed property compliance committee
  - Use of the Social Security Death Master File
  - Policies in force due to their non-forfeiture provision
  - Engage an independent specialist to assist

Examples of Best Practices

- Determine potential unclaimed property exposure
- Perform early outreach to payees as a first round of due diligence prior to the statutory due diligence period
- Get into compliance with applicable state requirements
- Develop and maintain centralized, detailed policies and procedures to identify, record and report unclaimed property
- Conduct internal audits of unclaimed property processes and procedures
- Form an unclaimed property committee that is responsible for compliance
  - Include key personnel, including, but not limited to, compliance, risk management, internal audit, legal counsel, upper management, treasurer, controller, IT, and tax director

Benefits of Compliance and Best Practices

- Strengthens relationships with state regulators
- Avoid assessment of penalties and fines
- Decreases your reputational risk and increase consumer confidence
- Location owners/beneficiaries can lead to long term marketing opportunities
- Maximize asset retention
- Accurate financial data
- Greater efficiencies that ultimately result in increased revenues, time and resources

Innovative Interpretations

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Inactivity: Potential Solutions

- Tracking owner-initiated activity
  - Website log ins
  - Customer Service call authentications
  - Receipt of written communications
  - Payment/Withdrawal request (excl. auto-transactions)
  - Cashed dividend/distribution checks
- Affirmative Contact Programs
- Handling Owners with Multiple Products
  - Activity on one asset sufficient to satisfy other assets?
  - Consolidated Account Statements

Audits: Potential Solutions

- Voluntary Disclosure Agreements
  - Formal/Informal – depending on the state
  - Controlled evaluation
    - Policies/Procedures
    - Records/Data - Sampling
    - Affirmative corrections
  - Independent consultant review
  - Limit lookback period – ie., 10 years
  - Voluntary remittance of unclaimed property
  - Avoid interest/penalties
  - Eliminate audit potential

Questions??

David L. Westmark

Sr. Counsel

Thrivent Financial

david.westmark@thrivent.com