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**Unclaimed Property**

Voluntary Disclosure Agreement programs, programs through which a holder can report on a voluntary basis its overdue unclaimed property, are commonly offered by states to encourage holders to come into compliance. In this article, Morris, Nichols, Arsht & Tunnell LLP's Michael Houghton and Donna L. Culver and Ryan LLC's Mark A. Paolillo and Susan Han discuss the availability and specifics of these programs in seven states.

**Unclaimed Property—Voluntary Disclosure Agreements**

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**I. Introduction to Voluntary  
Disclosure Agreements**

**A** voluntary disclosure agreement program, also known as a VDA, is a program through which a holder can report on a voluntary basis its overdue unclaimed property. Commonly offered by states to encourage holders to come into compliance with their un-

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claimed property reporting obligations, most VDA programs offer valuable benefits frequently unavailable to holders undergoing the more traditional unclaimed property audit, both in terms of time and expense.

Although their specific terms vary, VDA programs generally enable companies to achieve compliance with their unclaimed property reporting obligations while avoiding the imposition of some or all of the interest and penalties that might apply in an audit. In addition, holders participating in a VDA program typically enjoy more abbreviated look-back periods than those that apply in the audit context, which may significantly reduce the holder's liability. Finally, participation in a voluntary disclosure agreement program may assist holders in proactively managing and maintaining their unclaimed property compliance on a going-forward basis.

VDA programs can be either formal or informal. Both types of programs generally involve the execution of a form voluntary disclosure agreement by the holder and the state, through which the holder agrees to complete a self-audit of its books and records and to file

past due reports and remit amounts due in exchange for a waiver—in full or in part—of penalties and interest.

Although the requirements of the informal VDA programs vary depending on the practices of the particular state involved, most formal programs include written guidelines or other requirements governing such matters as the length of the look back period, the statistical methodologies to be applied in calculating the holder's liability and the deadline and format required for the written submission by the holder. Upon completion of the VDA, many states provide for the execution of a written agreement between the holder and the state which identifies the holder's liability and the legal entities, transaction years and property types discharged, and addresses the holder's ongoing reporting obligations and the state's ability to audit the holder to verify the accuracy of the VDA submission.

## II. Analysis of VDA Programs In Selected Key States

This article discusses the availability of VDA programs in seven key states: California, Delaware, Florida, Illinois, Michigan, New York, and Texas.

**California.** At the present time, California does not offer a VDA program under the California Unclaimed Property Law (UPL).<sup>1</sup> However, experience with California authorities has shown that holders who file past due property with the state are almost never assessed penalties, although interest is assessed by the State Controller's Office (SCO) and is rarely waived. A summary of this practice appears in a recent publication of the SCO's Unclaimed Property Division, which states that "[u]nder California law, the assessment of interest is mandatory for failure to report, pay, or deliver unclaimed property on time, unless there is a showing of reasonable cause for the delay."<sup>2</sup> Thus, Section 1577 of the UPL essentially provides that if a person fails to report, pay, or deliver property within the time periods prescribed by the UPL, interest is assessed at 12 percent per annum from the date the property should have been reported, paid, or delivered, unless the failure is due to "reasonable cause."<sup>3</sup> Although the term "reasonable cause" is not defined in the UPL, it is defined in regulations of the SCO. That regulation provides that reason-

able cause ". . . means the exercise of ordinary business care and prudence," and provides two examples as to what would be viewed as reasonable: (i) in the absence of willful neglect, failure was due to circumstances beyond the holder's control, and (ii) the failure was due to erroneous information given to the holder of unclaimed property by an employee of the Controller's Office.<sup>4</sup>

**Delaware.** Holders of abandoned and unclaimed property due to the State of Delaware can enroll in one of two voluntary disclosure agreement programs operated under the auspices of the Delaware Department of Finance and the Delaware Department of State, respectively. Under the Department of Finance program, a holder may come forward to report its past due unclaimed property liability for transaction periods dating back to 1991,<sup>5</sup> provided that a holder, which includes any subsidiary and all related entities, which has received an audit letter or which is already under audit, is not eligible for participation in the program. Upon acceptance into the program following completion of the required Form AP DE-1, the holder must complete a self-review of its books and records, file reports and pay all abandoned property due within six months. Upon completion of the review, the holder and the state execute a form AP DE-2, which identifies the property remitted, for which the holder receives a release for the report years covered by the agreement and for all preceding report years, subject to the state's ability to audit for an 18 month period. In the event that such audit discloses that the holder has failed to act in good faith or has materially failed to disclose the full amount of its abandoned and unclaimed property liability for the periods covered by the VDA, the AP DE-2 provides that it shall be deemed null and void, and the state may in its discretion, expand the scope of the audit to cover years prior to those covered by the VDA, and assess interest and penalties on all property found to be due and owing.<sup>6</sup>

Since 2012, the Delaware Department of State has also operated a voluntary disclosure agreement program through which holders can report past due unclaimed property, without threat of an audit, interest, and penalties. As originally conceived, this program was set to expire in June 2014, but was thereafter extended and made permanent by legislation enacted in 2015. Under this program, the Delaware Secretary of State is authorized to resolve and compromise claims for abandoned property otherwise owing to the State Escheator under the Delaware escheat law. Pursuant to that program, the Secretary of State may invite a holder, not currently under audit by the State of Delaware, to enter into a voluntary disclosure agreement with the Secretary of State, failing which the statute provides that the holder will be referred to the State Es-

<sup>1</sup> In reviewing the UPL, as well as past experience of the authors, California did offer an unclaimed property amnesty program years ago. Thus, Sec. 1577.5(a) of the UPL, as reviewed on LEXIS on May 10, 2016, stated that "Section 1577 does not apply to, and interest may not be imposed upon, any escheated property paid or delivered to the Controller at any time on or before Dec. 31, 2002." Furthermore, Sec. 1577.5(e) of the UPL essentially states that the Controller was to provide a report to the Legislature on the amnesty program, including, but not limited to, the amount of property surrendered thereunder, as well as identities of the holders participating in the amnesty program.

<sup>2</sup> See SCO's 2015 Summer Holder Newsletter, which can be accessed on the SCO website, which is available by accessing [www.unclaimed.org](http://www.unclaimed.org), the NAUPA website, or [www.sco.ca.gov](http://www.sco.ca.gov). The website materials cite Calif. Code of Civil Procedure Sec. 1577 as authority for the statements.

<sup>3</sup> See Calif. Code of Civil Procedure, Part 3, Title 10, Ch. 7, Art. 6, Sec. 1577. Penalties for failure to file reports, or pay or deliver property within the time periods prescribed by the UPL, are delineated in Sec. 1576 of the UPL.

<sup>4</sup> See Calif. Code of Regulations, T. 2, Div. 2, Ch. 2, Subch. 8, Art. 4.7, sec. 1172.90-Reasonable Cause-Defined.

<sup>5</sup> As a result of legislation enacted in 2015 requiring the State Escheator to promulgate a manual related to the conduct of voluntary disclosure agreements and escheat examinations to ensure fair and uniform treatment of holders of unclaimed property, the State Escheator has recently proposed a set of new regulations which, if enacted, would, among other things, establish a rolling 19-year look back period from the year of enrollment beginning Jan. 1, 2017.

<sup>6</sup> Form AP DE-2.

cheator for audit.<sup>7</sup> Holders who enter the Secretary of State's program prior to Dec. 31, 2016, and enter into a payment plan within two years of the state's acceptance of the holder into the program receive a shortened look-back period to 1996, while holders that enroll on or after Jan. 1, 2017, and enter into a payment plan within two years of acceptance receive a rolling 19-year look back. Like the program operated by the Department of Finance, the Secretary of State's VDA program is not open to any holder under audit by the State of Delaware or to holders previously enrolled in a voluntary disclosure agreement with the Secretary of State which previously withdrew from the program or which were removed by the Secretary of State for failure to work in good faith to complete the VDA program.<sup>8</sup>

Holders enter into a VDA with the Secretary of State by completing a Form VDA-1, which provides that the holder will pay any abandoned or unclaimed property due or enter into a plan for its payment within two years of the date on which the VDA-1 is executed. Upon completion of the VDA, the state and the holder execute a Form VDA-2, which provides for a release of all past due unclaimed property liability and a waiver by the state of the right to audit for all prior report years for property types reported, subject to the holder's agreement to file annual reports with the state listing its abandoned and unclaimed property liability in each of the three years succeeding the completion of the VDA.

**Florida.** Florida offers holders a formal VDA program. To participate in that program, the holder must not (i) be currently under examination or audit by the Florida Department of Financial Services, Florida Bureau of Unclaimed Property (the department), or by one of the department's contract auditors; (ii) have filed an annual report of unclaimed property with the department; (iii) have agreed to a department-assisted or contractor-assisted self-audit; (iv) have been requested to conduct a department-assisted or contractor-assisted self-audit; or (v) have been contacted by the department or by one of the department's contract auditors to schedule or to conduct an examination or audit of the holder.

There are a number of general requirements a holder must satisfy as part of the VDA. First, a holder must complete and execute a voluntary disclosure agreement and provide the department the following information in connection therewith: (a) name of entity, mailing address, contact person, telephone number, facsimile number and email address of the contact person, federal employer identification number, and standard industrial code classification; (b) the holder's state of incorporation; (c) the holder's principal place of business (city and state); (d) if the holder's state of incorporation and principal place of business is outside of Florida, the holder must provide a list detailing the cities in Florida where the holder conducts business with the number of locations in each city; and (e) if the holder has no locations within Florida, the holder must so state.

The holder must likewise submit a detailed plan outlining the disclosure process to be completed, which in-

cludes, at a minimum, a description of the procedures to be followed during the self-audit, the property types to be reviewed or audited, and the sampling and/or estimation techniques employed. If estimations are involved in determining the amounts to be reported, the calculations for the estimations must be reviewed and approved by the department prior to the acceptance of the property by the department and waiver of penalties. In the event that sampling and/or estimating are required due to inadequate records, the holder must submit an affidavit, signed by an officer of the holder, so stating. Upon completion of the VDA, the holder must file annual unclaimed property reports required by the Florida Unclaimed Property Act (UP Act). If the holder makes any false or misleading representations to the department, fees and penalties will be assessed as allowed by law, and the department may commence any other actions permitted by law.

The Florida VDA insulates holders from any penalty or interest against the holder for the reported property. The holder is also relieved of liability upon payment and delivery of the unclaimed property as provided in Section 717.1201 of the Act; however, this release of liability applies only to the type of property reported and remitted and is not a general waiver of all liability for all types of property. Upon receipt of the report and remittance, the department may still assert its right to conduct an examination of the holder's records pursuant to Section 717.1301 of the UP Act.

Upon receipt of the signed VDA and required information, the department will review and make a determination as to whether the holder's participation in the program will be approved. If approved, the department will sign the VDA, and a final order will be entered, binding the department and the holder to the terms and conditions of the VDA. Within three months thereafter, the holder must submit a detailed plan to the department consisting of the following information: (a) an outline of the disclosure process to be completed by the holder; (b) estimation calculations; and (c) an unclaimed property report (submitted on the required forms) consisting of the required reporting periods identifying the unclaimed property due to the department, including the funds for the prior ten report years.

As part of the final order, the holder must waive any right to (i) separately stated findings of fact and conclusions of law; (ii) receipt of a notice of rights; (iii) an administrative hearing or issuance of a recommended order; (iv) contest in any judicial or administrative forum the validity of any term, condition, obligation, or duty expressly created by the final order; and (v) object to or challenge in any judicial proceeding any express provision or requirement of the final order. In exchange, the department agrees that it will not use the VDA or final order against the holder as the sole basis for any future action, although, the department reserves the right to pursue any administrative or judicial action or remedy if there is any misrepresentation or fraud involved in the reporting of unclaimed property for any of the report years.

**Illinois.** Illinois also offers holders a formal VDA program. To participate in the program, the holder must (i) not be under examination by the Officer of the Illinois State Treasurer, Unclaimed Property Division (the Treasurer) or an agent of the Treasurer; (ii) conduct a self-audit of its books and records and file a report of findings within six months of the execution of the VDA

<sup>7</sup> 12 Del. C. § 1177(b).

<sup>8</sup> The program is likewise unavailable to any holder that entered into a voluntary disclosure agreement with State Escheator on or before Jan. 30, 2012, except as to property types or periods not included in such agreement.

for the period required for the presumptive abandonment plus the nine years immediately preceding the beginning of the period; (iii) file a report for the current reporting period in a timely manner; (iv) be able to provide supporting documentation for any estimation techniques used—the Treasurer must approve the estimation techniques before any estimated remittance is made and penalties are waived;—(v) be able to accept the VDA without modification.<sup>9</sup>

The holder is required to submit its remittance on form UPD601 and include owner details in an electronic format approved by the Treasurer.<sup>10</sup> The report and subsequent monetary findings are due to the Treasurer no later than six months from the date the VDA is signed by the Treasurer,<sup>11</sup> and the Treasurer maintains the right to perform an examination of the holder's books and records to determine the holder's unclaimed property obligations for the longer of 14 years or from the holder's date of incorporation, whichever is older (the examination period).<sup>12</sup>

For a holder participating in the VDA, all fees, penalties, and interest otherwise attributable to holder's unclaimed property obligation for the examination period will be waived by the Treasurer if the holder is in compliance with the Illinois Uniform Disposition of Unclaimed Property Act, 765 ILCS 1025 (Illinois UP Act).<sup>13</sup>

Upon completion of the VDA, the holder will need to maintain records enabling it to annually report the names and addresses of individuals for whom it is required to report unclaimed property, as failure to maintain such records following the execution of the VDA renders the VDA null and void. Furthermore, if any of the representations made by the holder in the VDA are false or misleading, the VDA will become null and void, and the Treasurer may assess any fees or penalties allowed by the Illinois UP Act and commence any other action permitted by law.<sup>14</sup>

**Michigan.** Michigan offers holders a formal VDA program. As indicated on the Michigan State Treasurer's website, under the heading "Reporting Unclaimed Property," the VDA program is open to holders who (i) have not previously reported unclaimed property to Michigan, or (ii) have underreported unclaimed property in the past.<sup>15</sup> The Michigan VDA is a particularly attractive one to holders, in that it only requires a look-back period of four reporting years, and states that holders who utilize the VDA will not be assessed penalties or interest.<sup>16</sup> Holders enter into a VDA by reviewing and completing Form 4689 (Rev. 09-14), titled "Michigan Unclaimed Property Voluntary Disclosure

Agreement," which is available for downloading on the Michigan State Treasurer's website. In reviewing Form 4689, the holder entering into the VDA agrees to five conditions prescribed by the state Treasurer's Office as follows:

(i) to accurately and timely file unclaimed property reports and remit payments for the current reporting year and the previous four reporting years;

(ii) to perform due diligence (i.e., notification to missing owners) valued at \$50 and greater as required by law;

(iii) to disclose all subsidiaries or entities that are part of the VDA;

(iv) to be fully compliant with the Michigan Uniform Unclaimed Property Act (Act) on a go-forward basis; and

(v) to file the reports using electronic reporting software in the nationally recognized NAUPA format.<sup>17</sup>

In return, the state agrees to certain key conditions. First, the state agrees that holders will not be assessed penalties or interest for property that is remitted voluntarily in accordance with the VDA and the Act.<sup>18</sup> Second, as indicated above, the "look-back" period for reporting is the previous four reporting years, plus the applicable dormancy period for the particular property type. When contrasted with the ten reportable years' "look-back" period Michigan delineates as applicable to unclaimed property audits, this is a significant concession. Finally, Form 4689 states that the Michigan Treasurer's Office agrees to exclude the holder from audit during the six-month period after the filing of such form.

As is the case with most states, a holder is not eligible for a Michigan VDA if (i) it is currently under audit, or (ii) it has been notified by the Michigan State Treasurer's Office or one of its contract auditors of Michigan's intention to conduct an unclaimed property audit.<sup>19</sup> As part of the required certifications under Part 4 of the VDA form, the authorized holder representative signing Form 4689 must confirm he/she is not under audit and has not been notified of an audit. In making a strategic business decision as to whether entering into a Michigan VDA makes sense, the above-mentioned factors should be taken into account. Significantly, the self-review done as part of the VDA process should thoroughly vet all possible property types that need to be reported. If the Treasury is not convinced that a thorough effort was made, it reserves the right, as provided in the VDA itself, to conduct a UP examination that "... may cover up to the last ten reportable years and result in an assessment of penalty and interest."<sup>20</sup>

In summary, the Michigan VDA program has several key provisions that make it very attractive to the holder community [i.e., (i) a look-back period of only four reporting years, plus applicable dormancy period, as com-

<sup>9</sup> See VDA, Sections 1 -10. Forms and formats for the Illinois VDA can be obtained at [www.treasurer.il.gov](http://www.treasurer.il.gov).

<sup>10</sup> See VDA, Section 4.

<sup>11</sup> See VDA, Section 4.

<sup>12</sup> See VDA, Section 5.

<sup>13</sup> See VDA, Section 6.

<sup>14</sup> See VDA, Section 8.

<sup>15</sup> This website can be accessed via either [www.unclaimed.org](http://www.unclaimed.org), which is the website for the National Association of Unclaimed Property Administrators ("NAUPA"), or <http://www.michigan.gov/treasury>.

<sup>16</sup> Note: When one adds the prescribed dormancy period, such as a three-year dormancy period for accounts payable or accounts receivable, to the prescribed reporting years, the look-back period becomes, for example, seven years for those property types.

<sup>17</sup> See Michigan Department of Treasury Form 4689 (Rev. 09-14), Part 2: Agreement Information. Form last reviewed on website on May 10, 2016.

<sup>18</sup> See Form 4689, Part 3: Treasury Agreement. Note: Michigan had a prior practice of assessing interest on past due property. However, in an email from the Michigan Unclaimed Property Administrator to Ryan AUP personnel on Jan. 20, 2015, it was indicated that the state would no longer be assessing interest on past due property submitted as part of a VDA.

<sup>19</sup> See Handbook for Reporters of Unclaimed Funds, "Voluntary Compliance."

<sup>20</sup> See Form 4689, Part 2: Agreement Information.

pared to a ten reporting year look-back period for an audit, plus applicable dormancy period, and (ii) waiver of penalties and interest]. As is the case with many states, the benefits of entering into a VDA should be balanced against the possibility that the holder could be subject to a subsequent audit after conclusion of the VDA. Thus, holders contemplating entering into the VDA should thoroughly review their books and records, and report all past due unclaimed property for the appropriate periods covered by the VDA.

**New York.** New York offers holders a formal VDA program. As indicated in the June 2015 Handbook for Reporters of Unclaimed Funds published by the New York State Comptroller's Office of Unclaimed Funds (OUF), the VDA program applies to first-time reporting organizations and, in some instances, to those who have filed in the past but who recognize that they have failed to report a particular type of property and have come forward voluntarily to correct the error.<sup>21</sup> Like other state VDAs, holders are ineligible for the VDA after being contacted by the OUF or its agent regarding an audit.

Holders initiate the VDA by either (i) filing the appropriate Abandoned Property Report directly with the OUF along with a cover letter indicating that the report is being filed under voluntary compliance, or (ii) filing a voluntary compliance agreement, which provides the holder with additional time to review its records and ensures that the holder is not contacted for audit in the interim.<sup>22</sup> The OUF determines whether an examination of the holder's books and records can be completed by self-audit or CPA firm-assisted examinations, or whether the OUF will conduct the examination.<sup>23</sup> This provides the holder with an opportunity to review its records and correct any issues of omission with respect to its reporting obligations to New York, as well as various other states. The holder will need to submit a voluntary disclosure proposal describing the methodology used in determining the amount due to the OUF within six months from the date of the executed VDA.<sup>24</sup> No remittance will be accepted by the OUF until the OUF provides the holder with its written agreement as to the methodology used in determining the amount due. If the holder desires to make an estimated payment and file an abandoned property report prior to finalization of any pending or new VDAs, it may submit a written request to the OUF. The OUF's acceptance of such request is predicated upon the understanding that the VDA process will not be considered finalized until the methodology used to determine the amount due has been accepted in writing by the OUF.<sup>25</sup>

According to the 2016 VDA, the examination and any resulting settlement agreement will cover the reportable periods from 1996 through 2016.<sup>26</sup> This includes unclaimed wages, accounts payable checks, refund checks, rebate checks issued and/or payable from 1992 to 2012 as well as other general ledger items issued

and/or payable from 1992 to 2012 and gift certificates sold between 1992 and 2010.<sup>27</sup> Specifically, the "reach-back" is as follows: (i) for all property other than general ledger items (e.g., debt, equity, reorganization, etc.) the applicable statutory floor date for the specific property type applies; and (ii) for general ledger items, including unclaimed payroll, vendor payments and checks, accounts payable and receivable credits, gift certificates, etc., where there has not been a willful attempt on the part of current management to conceal the abandoned property in question, a reach-back to Jan. 1, 1992, applies.<sup>28</sup>

In the event a settlement agreement is reached based upon the company's own review, the OUF reserves the right to conduct an examination of relevant books and records within two years from the later of the settlement agreement date or the date of payment to the OUF by the company.<sup>29</sup> In the event a settlement agreement cannot be reached, the negotiations conducted will not be treated in any respect as an admission of reporting liability by the company. No interest or penalties will be imposed on the company with respect to the unclaimed property payable to the OUF under the terms of any resulting settlement agreement.

An erroneous or misrepresentation of facts or failure to make full disclosure by the holder during the VDA process shall provide the OUF with a basis for nullification of the VDA in whole or in part.<sup>30</sup> Furthermore, the holder will need to agree to notify the OUF regarding any property reportable to New York or identifiable to a New York resident that has been reported to or claimed by any other state. The holder must also agree to maintain and retain accurate books and records on an ongoing basis, which will enable it to identify all unclaimed property subject to the New York State Abandoned Property Law (APL) (including but not limited to owner name, address, origination date, and amount) and file complete and accurate Abandoned Property Reports annually in the future, as required under the APL.<sup>31</sup> Prior to remitting property to the OUF, the holder will conduct all required due diligence as set forth in Section 1422 of the APL. For example, at least 90 days prior to the final report/remittance, all holders are required to send a first class mailing to each person whose name is expected to appear on the report unless the address is unknown, or the address on record is demonstrably undeliverable.<sup>32</sup> In addition, at least 60 days prior to the final report/remittance, a certified mailing, return receipt requested, should be made to each person expected to appear on the report whose abandoned property is valued in excess of \$1,000.00, unless a claim has been initiated since the first class mailing was sent, or the first class mailing was returned as undeliverable.<sup>33</sup> It should be noted that the OUF will not accept any report or check until the statutory due diligence requirements have been completed.

All pending or open VDA proposals should be updated to include property due up to the filing year. All applicable due diligence must be performed in a timely

<sup>21</sup> The Handbook for Reporters of Unclaimed Funds (NY Handbook) can be accessed at [www.osc.state.ny.us/ouf/oufhandbook/files/oufhandbook.pdf](http://www.osc.state.ny.us/ouf/oufhandbook/files/oufhandbook.pdf).

<sup>22</sup> See NY Handbook.

<sup>23</sup> See VDA, Section 1.

<sup>24</sup> See VDA, Section 3.

<sup>25</sup> Id.

<sup>26</sup> This is based on the 2016 VDA. See VDA, Section 4.

<sup>27</sup> Id.

<sup>28</sup> See the NY Handbook.

<sup>29</sup> See VDA, Section 6.

<sup>30</sup> See VDA, Section 7.

<sup>31</sup> N.Y. Aband. Prop. §§101 – 1502.

<sup>32</sup> See Section 1422(1) of the APL.

<sup>33</sup> See Section 1422(2) of the APL.

manner. If the holder's current-year abandoned property report is not due at the time the VDA is finalized, the holder is required to file the report in a complete and timely manner.

The VDA expires six months from the date it is signed by a duly authorized representative of the OUF; however, an extension request may be submitted in writing prior to the expiration date.<sup>34</sup> Such extension request must provide specific details of the work performed, the estimated completion date, and an explanation as to why additional time is required. An extension request is only valid with the written consent of the OUF, and the failure to obtain such written consent may result in nullification of the extension.

**Texas.** Texas offers holders a formal VDA program. However, before analyzing the details of the VDA program offered by the Texas State Comptroller's Office, an important caveat must be made. Perhaps unlike any other state, Texas requires that, as a condition precedent to completion of a successful unclaimed property VDA, a holder must be in compliance with all Texas state taxes.<sup>35</sup> This is perhaps explained by the fact that the Texas State Comptroller's Office is responsible for compliance with unclaimed property, as well as with other Texas state taxes. Thus, before a particular holder seeks to enter into a Texas VDA, individuals responsible for unclaimed property compliance should carefully check with their tax department personnel to ensure they have been complying with Texas state tax laws. If the holder is not in compliance with Texas state tax laws, it may not be advisable to file a VDA with the Texas Comptroller's Office.

Per recent discussions with representatives of the Texas Comptroller's Office, a VDA request may be initiated in one of two ways: (i) a holder may contact the Holder Reporting section of the Unclaimed Property Division of the Texas Comptroller's Office, or (ii) an email can be sent to [up.vda.requests@cpa.texas.gov](mailto:up.vda.requests@cpa.texas.gov). Once the request is received, the Texas Comptroller's Office will review the initial request and, absent a reason not to do so, will send a VDA form to the applying entity, along with a Texas Nexus Questionnaire to be completed by each of the affiliates sought to be included in the VDA.<sup>36</sup>

<sup>34</sup> See VDA, Section 14.

<sup>35</sup> See, e.g., Section 2(b) of Voluntary Disclosure Agreement furnished by Texas State Comptroller personnel to Ryan AUP personnel recently, in which it is stated: "If, within 180 days following the effective date of this Agreement, Comptroller discovers that . . . Holder is not in compliance with reporting or remitting requirements for other state taxes, not disclosed pursuant to this Agreement, then this Agreement may be rescinded at the Comptroller's election upon 10 days written notice to the Holder." Note: Unlike a number of states, Texas does not maintain a sample or template VDA on its unclaimed property website. Rather, the form of agreement to be used in a VDA for a specific client may be requested from the Texas Comptroller's Office.

<sup>36</sup> See Texas Nexus Questionnaire, Form AP-114 (Rev. 5-12/16); such Form last reviewed on website on May 10, 2016. In addition, recent correspondence between the Texas Comptroller's Office and Ryan AUP indicates that if the VDA is meant to cover more than one legal entity, then one is to include a "list of affiliates that will be included in the VDA and their Federal EINs." Note: Based on recent discussions between representatives of the Holder Reporting Section, Unclaimed Property, Texas Comptroller's Office, and Ryan AUP, responsibility for

The questionnaire is designed to provide the Comptroller's Office with more information on the applicant and affiliates, types of activities they've been conducting in Texas, types of tax permits or licenses issued to the entity by the Texas Comptroller, etc. Other requirements, such as compliance with due diligence requirements, should also be observed.<sup>37</sup> Upon receipt of the completed VDA and Texas Nexus Questionnaire, the Texas Comptroller's Office conducts a review process to verify that the holder and the affiliates mentioned in the VDA are indeed eligible to enter into a VDA. If so, a VDA is executed by the Texas Comptroller's Office and returned to the holder with applicable information necessary to report the unclaimed property for the appropriate disclosure period.

Highlights of the VDA form are as follows. First, based on both recent dealings with representatives of the Texas Comptroller's Office, as well as prior VDAs, reports must be made for the current report year, and for a look-back period of ten prior report years, plus applicable dormancy years for each property type. Second, the holder is expected to "fully report and remit all unclaimed property data and funds" within 180 days of the effective date of the VDA.<sup>38</sup> Third, if the Comptroller discovers that within 180 days following the effective date of the VDA, the holder had either (i) been informed prior to the effective date of the VDA of the Comptroller's intent to conduct an audit or investigation of the holder, or (ii) not been in compliance with reporting or remitting requirements for other state taxes, then the Comptroller is entitled to rescind the agreement for the VDA.<sup>39</sup> Fourth, the Comptroller generally agrees to waive both penalties and interest with respect to property timely paid in full; provided, however, the VDA states that if a previous State Treasurer or Comptroller audit or investigation reflected a history of similar omissions or errors by the holder in reporting and/or remitting unclaimed property, then only penalties may be waived.<sup>40</sup>

At the time the holder is considering the execution of the prescribed VDA form, it also must be considering the Texas Nexus Questionnaire form furnished by the Comptroller. The form generally is designed to familiarize the Comptroller with the VDA applicant's activities in Texas over the past seven years. For example, Question 12 of the form asks the "start date" for various activities in Texas over the past seven years, such as performance of any contracts, whether items were sold and delivered in Texas in company vehicles, any warranty work done in Texas, any real property acquired in

issuance of VDAs has recently been transferred from the Texas Business Activity Research Team (BART) group in the Comptroller's Office to the Holder Reporting Section, Unclaimed Property, in the Comptroller's Office. However, our understanding is that the Holder Reporting Section coordinates with BART with respect to review of "other state taxes," which, as indicated above, is an area closely reviewed by Texas authorities.

<sup>37</sup> Based on recent correspondence between the Texas Comptroller's Office and Ryan AUP, the holder is asked to confirm: (i) that all due diligence requirements have been met prior to remitting the unclaimed property, and (ii) that remittances of unclaimed property have not been reduced by any service or maintenance fees.

<sup>38</sup> See VDA, Section 1.

<sup>39</sup> See VDA, Section 2.

<sup>40</sup> See VDA, Section 8.

Texas, any personal property used or located in Texas, etc. A full description of the entity's activities in Texas is requested. In summary, utilization of the Texas Comptroller's VDA can be very beneficial for holders. However, the key caveat is that a holder needs to ensure it is in compliance with Texas state taxes before commencing the VDA process. Thus, for many entities seeking a Texas VDA, holders are well advised to check with their tax, legal, purchasing, and possibly other departments or units of the company before applying for the VDA.

### III. Conclusion and Recommendations

In summary, it appears, as indicated by the recent Delaware VDA legislation, that VDAs are likely to become an increasingly important part of the holders' unclaimed property compliance toolkit. The advantages of the VDA, as indicated above, can be significant, if utilized properly. The authors suggest the following recommendations to assist in the proper utilization of VDAs by the holder community.

- **Use Only After Thorough Review.** Holders should only consider entering into a VDA after a thorough vetting of their books and records, preferably with assistance from a consulting firm and law firm that have substantial experience in the area. Given that the results of the VDA may be tested, so to speak, by a subsequent state audit, it behooves holders to get it right the first time, and make a detailed, thorough review of their books and records. For example, in one case a holder, believing it only had about \$3.6 million in unclaimed property, made an offer of the same to Delaware to settle a Delaware VDA. When the matter was unable to be settled via the VDA, years of litigation ensued, with the holder finally agreeing to a settlement of \$17.65 million.<sup>41</sup>

- **Know Each State's Eligibility Rules.** Each state has different rules governing eligibility for its VDA program. As a general rule, if a holder is either under audit or has been notified by the state or its contract auditor agent that its being placed under audit, the holder is ineligible to participate in the VDA. Some states, like Delaware, may not allow a holder to enter into a VDA if it has previously entered into an unclaimed property VDA with the state.<sup>42</sup> Texas, as was indicated earlier, reserves the right to rescind the VDA if it discovers within 180 days following the effective date of the agreement that the holder was informed prior to entering into the VDA of the Comptroller's intent to conduct an audit of holder.<sup>43</sup>

- **Understand Time Period to Conduct VDA.** Each state has expectations surrounding when it expects holders to finish their reviews and report and remit property to the state. In states that have an "informal VDA" process, it is critical that this point be negotiated as early as possible because the state is likely not to have written guidance delineating what that expectation may be. For example, many states provide a six-month deadline to

complete the VDA process but are generally liberal about granting extensions, based on the facts and circumstances. With respect to "formal VDA" states, our experience has been that most states are receptive to consideration of extensions of their stated time periods in which they expect the work to be completed. However, if longer periods are needed, our experience is that it is important to communicate the request for a longer period "sooner than later."

- **M&A Considerations.** In some situations, a holder may have undertaken a major acquisition and, after the "dust has settled," come to realize that the acquired entity did not report unclaimed property in a satisfactory manner. This can be a good situation to utilize a VDA. For example, the recent Delaware legislation states that even if a holder had entered into a prior VDA with Delaware such that the holder was not eligible to enter into another VDA, if the holder had "subsidiaries or related entities" that were not part of the prior VDA, those entities would be eligible to essentially enter into a new VDA.

- **Be Cognizant of Possible Federal Preemption Defenses.** It is important to have access to legal advice with regard to areas where federal law or regulations may provide an affirmative defense such that the funds in question are not escheatable by the states. Examples of laws that should be considered include, but are not limited to, federal pension law (ERISA), federal bankruptcy law, and federal transportation and telecommunications laws.

- **Consider Contracts With TPAs, Claims Administrators, and Transfer Agents.** It is important to carefully review contracts a holder has with third-party administrators (TPAs), claims administrators, and transfer and dividend paying agents. For example, some companies outsource the payroll function to a third party. By way of further example, many publicly held companies utilize transfer and dividend paying agents, while other companies utilize TPAs or claims administrators to handle payment under some of their benefit plans. The authors' experience has been that many contracts with TPAs or claims administrators for handling of certain benefits property do not delineate who has responsibility for compliance with unclaimed property laws. As such, the attendant result is that no one is monitoring such compliance, and it "falls through the cracks." Once the responsibilities are spelled out in the contract, holders should take steps to periodically monitor the activities of these entities with regard to unclaimed property compliance.

- **Retention of Proper Records.** Whether preparing a VDA or defending a state unclaimed property audit, retention of proper records can provide the best defense for presenting and defending one's case in this area. Most states have unclaimed property record retention requirements that are longer than those required in other areas.<sup>44</sup> In addition, many states require that a holder agrees in the VDA to keep and preserve records. For example, Texas requires as part of its VDA that a holder "...keep and preserve suitable records of unclaimed property for ten years from the due date of the return. . . ."<sup>45</sup>

<sup>41</sup> See Michael Houghton, *et al.*, *Unclaimed Property*, 74-3d Corporate Practice Series (BNA-Rev. 2014), at pp. A-15-16 for a more detailed discussion of the *Computer Associates Inc.* case.

<sup>42</sup> See earlier discussion for analysis of new rules governing eligibility for a Delaware VDA with the Delaware Secretary of State's Office.

<sup>43</sup> See VDA, Section 2.

<sup>44</sup> See the above-mentioned BNA treatise, at pp. A-57-59 for a more detailed discussion of these requirements.

<sup>45</sup> See Texas State Comptroller VDA, Section 5.

■ **Releases.** Understand exactly what type of release the state is granting in the VDA. For example, Texas states in its VDA that “[c]ontingent upon holder’s good faith compliance with this agreement, Comptroller releases holder from all actual or potential liability for all unclaimed property reported under this agreement.”<sup>46</sup>

■ **De Minimis Rule.** If the thorough review step mentioned above indicates that only a de minimis amount of past due property is owed to a particular state that is past due, it may make sense to forego a VDA for that particular state and include that amount with a current report for such state. If that is done, an explanation should be provided with the report explaining the situ-

ation involving the past due property. There is no “bright line” test for the exact amount that qualifies as “de minimis” for purposes of this rule. Rather, a number of facts and circumstances need to be evaluated on a case-by-case basis, including, but not limited to, the amount of past due property involved, the particular property type involved, the length of time for which it may be considered delinquent, the underlying reason associated with why it was not reported in a timely fashion, and the particular state involved.

In conclusion, VDAs are becoming an increasingly important part of holders’ unclaimed property compliance options. If used properly, they can assist in seeing that penalty and interest payments are minimized and that property that may have previously been inadvertently overlooked gets reported in a proper fashion.

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<sup>46</sup> See Texas State Comptroller VDA, Section 3.