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Escheat

Del. High Court's Input Sought On State's Escheatment Law

The U.S. District Court for the Southern District of New York Jan. 29 asked the Delaware Supreme Court to weigh in on the proper interpretation of the Delaware statute governing escheated property—in this case, the plaintiff's stock in a Delaware corporation, the price of which rose dramatically after it was sold by the state (*A.W. Financial Services S.A. v. Empire Resources Inc.*, S.D.N.Y., Docket No. 1:07-cv-08491, 1/29/09).

According to Michael Houghton, a partner at Morris, Nichols, Arsht & Tunnell LLP in Wilmington, Delaware, the case was docketed in the Delaware Supreme Court on Feb. 5, 2009. Houghton, who is a co-author of BNA's Corporate Practice Series portfolio on unclaimed property, stated that as of Feb. 8, the Court had not accepted the Southern District of New York's certification request—and the Court has the discretion not to accept the request. He also indicated that if it is accepted—and he expects a decision on that soon—it is likely that the briefing will take three months and then the Court would probably set the case for oral argument shortly thereafter.

As the legal home of so many *Fortune* 500 companies, Houghton noted that Delaware is a critical fo-

rum for the development of unclaimed property law. He said a decision in this case could have a significant impact on corporations, shareholders, and intermediaries who handle shares for both.

The district court noted that stock often escheats to the issuing company's state of incorporation and that this action "raises important and novel questions about Delaware's escheat law."

The court also noted that the Delaware legislature recently amended the state's escheat law to reduce the period of dormancy before a stock becomes escheatable from five years to three years, which "may lead more shareholders to bring suits such as this one, alleging that the stock's issuer or a transfer agent violated the escheat law."

The court recounted that in 1994, plaintiff A.W. Financial Services S.A., then known as Tertiare Investissement S.A. and Tertiare Development S.A., bought 40 shares of Integrated Technology USA Inc. Thereafter, Integrated merged with Empire Resources Inc., a Delaware corporation. As a result of the merger, Tertiare's 40 Integrated shares became 30,426 shares of Empire.

In 2000, Tertiare wrote to Empire inquiring about its shares. It received a response from defendant American Stock Transfer & Trust Co., Empire's transfer agent, acknowledging its—Tertiare's—"loss" of its Empire stock certificate. It asked Tertiare to submit a loss affidavit and to purchase a surety bond,

after which American Stock said it would provide a replacement stock certificate.

In fact, the court noted, Tertiare had not lost its original stock certificate; "it had never gotten one in the first place. . . . Nevertheless, Tertiare agreed to submit the requested affidavit and to purchase the surety bond. . . . It received a replacement certificate from American Stock less than a week later."

Wrongful Escheatment?

In 2004, four and a half years later, Tertiare's Empire shares were turned over to the state of Delaware as escheated property, allegedly, either directly by Empire or through American Stock.

In 2006, A.W. Financial wrote to Empire "asking that its shares be re-registered under its new name." Shortly thereafter, A.W. Financial learned that Tertiare's Empire shares had been escheated to Delaware.

In its lawsuit, A.W. Financial contended that its shares were turned over to the state in violation of the escheat law, under which stock does not qualify as escheatable until it has been dormant for at least five years. It claimed that when Tertiare started communicating with the defendants about the replacement stock certificate, the clock on the five-year dormancy period was restarted. The shares, however, were escheated only four years and five months after the replacement certificate was issued.

According to the court, once A.W. Financial contacted the state about the wrongful escheatment, Delaware remitted the money it made when it sold the securities. However, the value of the shares allegedly rose dramatically after they were sold—from approximately \$4 per share to approximately \$58 per share.

A.W. Financial contended that the premature sale of its shares, resulting from the defendants' incorrect conclusion that the stock was escheatable, caused it at least \$870,487 in damages. The defendants argued that A.W. Financial failed to state a claim upon which relief may be granted,

and that in any event, they are immune from suit under the Delaware escheatment law.

Questions Asked

The district court decided to ask the Delaware Supreme Court the following questions:

- whether the June 30, 2008, statutory amendment to the “period of dormancy” (which changed that period from five years to three years) applies retroactively in civil actions involving stocks escheated prior to that date;

- under what legal theory, if any, can the plaintiff base a civil action against the defendants that they incorrectly determined that the stock was escheatable and was improperly transferred to the State of Delaware: negligence, conversion, breach of fiduciary duty, “failure to register,” or some other cause of action;

- whether the statute’s immunity provisions apply under these circumstances; and

- what allegations are sufficient to plead that a party did not act in “good faith” and thus is not entitled to immunity under the law.