An Examination of Unclaimed Property Laws After the Adoption of RUUPA: Suggestions for Continued Advancement

THE AMERICAN BAR ASSOCIATION SECTION OF TAXATION, STATE AND LOCAL TAXES COMMITTEE*

Abstract

While taxes have been imposed for several millennia, the modern unclaimed property laws are of more recent vintage and the underlying legal concepts are less developed. The unclaimed property law unquestionably has become controversial in recent times. The states can present powerful stories detailing when assets were recovered for owners under state unclaimed property laws. At the same time, some audits, especially multistate contingent-fee audits, have asserted very large recoveries against holders by means that caused the holders to object strongly to the methods employed in the audits.

This Article is a response to the Revised Uniform Unclaimed Property Act of 2016, commonly known as "RUUPA," issued by the Uniform Law Commission. The Article discusses elements of RUUPA that should be reconsidered.

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I. Introduction

While taxes have been imposed for several millennia, the modern unclaimed property laws are of more recent vintage and the underlying legal concepts are less developed.[1] For example, it is well understood that the states "stand in the shoes of the owners"[2] of the property for purposes of claiming a right to the property that is superior to that of the person who possesses the property—the "holder." This concept, which is described as the "derivative rights doctrine," raises fundamental questions as to whether the holder can raise all the defenses, for example, asserting statutes of limitations against the states that the holder could have asserted against the owner.

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[1] Unclaimed property laws are sometimes referred to as "escheat," which is a longstanding part of common law, but the two concepts are distinct. Escheat contemplates that the state is taking ownership of the property when no heirs or other legal successors to the property can be located. The modern unclaimed property laws contemplate custodial rather than ownership systems by which the states hold the property with the goal ultimately to return the property to the owners. In practice, some of the property that is transferred to the states effectively escheats to the states for want of a private claimant for the property. The amounts that the states currently retain represent billions of dollars.

[2] *See, e.g.*, *In re* Steins Old Harlem Casino Co., 138 F. Supp. 661, 666 (S.D.N.Y. 1956) ("The state's right of escheat is the right of an ultimate heir; it does not assert a separate claim to the fund but stands in the shoes of those so-called unknown creditors who are deemed to have abandoned their claims. Such creditors, by diligence, can cut off the rights of other claimants, and the state, standing in their shoes, has the same right."); Petition of Abrams, 512 N.Y.S.2d 962, 968 (Sup. Ct. 1986) ("The State, in asserting the right of escheat, stands in the shoes of the rightful claimants, and is entitled to reclaim the funds as abandoned property."); S.C. Tax Comm'n v. Metro. Life Ins. Co., 221 S.E.2d 522, 524 (S.C. 1975) ("The Commission's rights under the act are derivative. It succeeds, subject to the act, to the rights of the abandoned property's owners. It takes only the interest of the absent or unknown owner."); Presley v. Memphis, 769 S.W.2d 221, 224 (Tenn. Ct. App. 1988) ("The state acts under the statute to protect the rights of the property owners. Any rights and obligations of the state in the property are derivative of the rights of the owners of the property.").

All the states have enacted unclaimed property laws. These state statutes, regulations, and the limited case law that interprets these state enactments do not tell the entire story. Two other critical sources of law are the federal common law announced by the courts, especially the United States Supreme Court,[3] and various iterations of the Uniform Unclaimed Property Acts (UUPA).

This Article will explore various principles of state unclaimed property laws to which the state statutes should adhere. Such a discussion is of paramount importance given the latest examination of unclaimed property law by the Uniform Law Commission, which is the Revised Uniform Unclaimed Property Act of 2016, commonly known as "RUUPA."[4]

A Subcommittee, and later a Task Force, of the American Bar Association (ABA) Tax Section's State and Local Taxes Committee have been monitoring RUUPA. The analysis was done in cooperation with the ABA Business Law Section. The Task Force concludes that, though some of the RUUPA provisions would advance the administration of unclaimed property laws in the states, the states should not adopt RUUPA because of significant concerns about some of RUUPA's provisions.

On February 5, 2018, the ABA House of Delegates indefinitely postponed a resolution to approve RUUPA as an appropriate Act for those states desiring to adopt the specific substantive law suggested therein. The State and Local Tax Committee Task Force supported that action by the House of Delegates. In this Article, members of the Task Force examine RUUPA, including provisions that persuaded the Task Force to conclude that, without changes to its terms, the states should not adopt RUUPA despite its approval by the Uniform Law Commission.

The unclaimed property law unquestionably has become controversial in recent times. The states can present powerful stories detailing when assets were recovered for owners under state unclaimed property laws. At the same time, some audits, especially multistate contingent-fee audits, have asserted very large recoveries against holders by means that caused the holders to object strongly to the methods employed in the audits.[5] Holders also have argued that the audit process was not likely to produce recoveries of property by the state that ever would have been made available to private claimants because no owner was ever identified for the property required to be turned over to the state.[6]

Because the unclaimed property law area is expanding in its reach and controversies seem to be increasing as well, the adoption of RUUPA and the

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[3] *See, e.g.*, Pennsylvania v. New York, 407 U.S. 206 (1972); Texas v. New Jersey, 379 U.S. 674 (1965).

[4] Revised Unif. Unclaimed Prop. Act (Unif. Law Comm'n 2016) [hereinafter RUUPA], http://www.uniformlaws.org/shared/docs/Unclaimed%20Property/RUUPA_Final%20Act_2016.pdf.

[5] *See, e.g.*, Temple-Inland, Inc. v. Cook, 192 F. Supp. 3d 527 (D. Del. 2016).

[6] *Id.*

failure to secure support from the ABA present an important opportunity to examine portions of RUUPA that could be improved. The Task Force looks forward to the time when the ABA could support adoption by the states of a revised RUUPA. It is in this spirit that the observations and recommendations concerning RUUPA are presented. At minimum, as states seek to enact RUUPA, principles addressed in this Article should be given due consideration and should inform possible changes to the provisions found in RUUPA.

II. History of Uniform Unclaimed Property Acts

Laws addressing unclaimed property have formed part of the American legal system since shortly after the Revolutionary War.[7] The underlying doctrines derive from English common law doctrines of escheat and *bona vacantia* (Latin for "vacant goods").[8] When the heir or legal successor of real property could not be found, the doctrine of escheat returned it to the crown.[9] But where personal property was apparently abandoned or lost or otherwise lacked an owner, it was subject to a right of appropriation by the crown.[10] By the late nineteenth century, state statutes mandated that personal property, sometimes including intangible personal property, could pass to the states.[11] Some states' laws provided for the state to conserve the property for the owner, while using it for the benefit of the state, until a statutory period passed and ownership passed to the state by escheat.[12] Others provided for the state to serve as permanent custodian, whereby the rightful owner could always assert the right to ownership and escheat never occurred.[13] The various states' laws were diverse and often incomplete.[14]

Enter the National Conference of Commissioners on Uniform State Laws (NCCUSL), a group of practicing lawyers, judges, legislators, legislative staff, and law professors appointed by state governments to draft and promote uniform state laws in various areas of law where uniformity is desirable.[15] The NCCUSL drafted a series of versions of laws on unclaimed property: the Uniform Disposition of Unclaimed Property Act of 1954 and 1966, and the Uniform Unclaimed Property Act of 1981 and 1995.[16] As stated

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[7] Maryann B. Gall, *Escheat: The Basic Rules, What the U.S. Supreme Court Dictated About Compliance Priorities, B-to-B Exemptions, Gift Card Planning Opportunities and Recent Case*s, 1 J. Payment Sys. L. 390, 391 (2005).

[8] Gall, *supra* note 7, at 391-92, 392 n. 2.

[9] Note, *Origins and Development of Modern Escheat*, 61 Colum. L. Rev. 1319, 1319-20 (1961).

[10] Note, *supra* note 9, at 1326.

[11] Note, *supra* note 9, at 1327; Gall, *supra* note 7, at 392.

[12] Note, *supra* note 9, at 1331.

[13] Note, *supra* note 9, at 1331.

[14] Gall, *supra* note 7, at 393.

[15] *See About the ULC*, Unif. Law Comm'n, last accessed Aug. 6, 2018, http://www.uniformlaws.org/Narrative.aspx?title=About%20the%20ULC.

[16] *See Unclaimed Property Act Summary*, Unif. Law Comm'n, last accessed Aug. 6, 2018, http://www.uniformlaws.org/ActSummary.aspx?title=Unclaimed%20Property%20Act.

by NCCUSL, UUPA "provides a system for transferring intangible personal property and personal property in safety deposit accounts, held by an entity other than the rightful owner, to the state when it is deemed abandoned by the rightful owner."[17]

NCCUSL's aims have been to increase consistency in the state laws in this area to help businesses engaged in interstate commerce, preclude claims by multiple states over the same unclaimed property (*i.e.*, multiple liabilities), prevent unjust enrichment by holders quietly holding intangible personal property that has been abandoned by its rightful owners, protect unknown owners by locating them and returning property to them, and provide the custodial state with revenue.[18] Unlike escheat, under UUPA only the custody of the property transfers to the state, not its ownership.[19] The state must continue to hold the property until the rightful owner claims it.[20] Though states do not own the property under UUPA, they may use it for the general benefit of their citizens while holding it.[21]

In 1954, the main concern was multiple liabilities, which UUPA proposed to resolve through reciprocity provisions.[22] Thus, each holder would be subject to no more than one liability for each property. NCCUSL revised UUPA in 1966 to address problems arising from money orders and traveler's checks, whose issuers could not know who ultimately was the holder of the instrument.[23] These versions of UUPA applied a contacts analysis to determine the priority of states' claims based on the degree of each state's relationship to the unclaimed property.[24] UUPA of 1981 wholly revised the prior acts.[25] Its main concern was to revise the priority rules by codifying the rules set forth in *Texas v. New Jersey*.[26] The basic rule is that the owner's state is the one entitled to custody.[27] If that state cannot be ascertained, the holder's state has secondary priority.[28] UUPA of 1995 incorporated further refinements to priority based on *Delaware v. New York*, which solved the question of whether secondary priority for investment securities should be the state where the

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[17] *See Description of Unclaimed Property Act*, Unif. Law Comm'n, last accessed Aug. 6, 2018, http://www.uniformlaws.org/Act.aspx?title=Unclaimed%20Property%20Act.

[18] *Unclaimed Property Act Summary*, *supra* note 16; Commentary, *The Uniform Unclaimed Property Act of 1981: Time to Abandon the 1966 Act in Alabama*, 34 Ala. L. Rev. 51, 53 (1983); Gall, *supra* note 7, at 393.

[19] *Unclaimed Property Act Summary*, *supra* note 16.

[20] *Unclaimed Property Act Summary*, *supra* note 16.

[21] Gall, *supra* note 7, at 393-94.

[22] Gall, *supra* note 7, at 393-94.

[23] Gall, *supra* note 7, at 393-94.

[24] Elizabeth Pitman, Scott M. Schiefelbein, & Sherridan S. Starr, *Escheat and Unclaimed Intangible Property (Part I)*, 1 Corp. Bus. Tax'n Monthly 21, 21-22 (2000).

[25] *Unclaimed Property Act Summary*, *supra* note 16.

[26] 379 U.S. 674 (1965); Gall, *supra* note 7, at 394; Commentary, *supra* note 18, at 55-60, 65.

[27] *Unclaimed Property Act Summary*, *supra* note 16.

[28] *Unclaimed Property Act Summary*, *supra* note 16.

issuing corporation was domiciled or the state where the investment intermediary was domiciled by choosing the latter as the party legally obligated to deliver the unclaimed property to its owner.[29] Changes in UUPA over time also involve: (1) the period of time after which property is deemed abandoned (dormancy period), which varies depending on the type of property; (2) the property to which the holder could apply dormancy charges for the owner's inactivity with respect to the property; and (3) how abandonment may be inferred.[30] The general trend has been to reduce the dormancy period from 20 years before UUPA, to seven years generally under UUPA of 1954, to five years generally under UUPA of 1981 and 1995.[31]

Uniformity in unclaimed property laws has remained an elusive goal, however. Initially, only a few states adopted UUPA of 1954.[32] Thirteen states and the District of Columbia initially adopted UUPA of 1966 (with modifications).[33] By the time NCCUSL adopted UUPA of 1981, the number of states that had adopted statutes based on some form of UUPA had increased to over 30.[34] Initially 33 states and the Virgin Islands adopted UUPA of 1981 (with modifications), and 15 states initially adopted UUPA of 1995 (with substantial modifications).[35] Despite the growing number of states adopting some form of UUPA, unclaimed property laws continue to vary widely among the states, such as in the various compliance requirements.[36] And several states have still not adopted any version of UUPA.[37] Many of the states that have adopted some version of UUPA contain modifications that treat certain types of property differently from any of the UUPA versions.[38]

In the 25 years since UUPA of 1995, stakeholders have identified a variety of problems with UUPA, including changes needed due to technological advances, and many have urged NCCUSL to revise UUPA.[39] After over three years of work on revisions, NCCUSL issued, in late 2016, a new Revised Uniform Unclaimed Property Act (RUUPA), which is the focus of this

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[29] Delaware v. New York, 507 U.S. 490 (1993); *Unclaimed Property Act Summary*, *supra* note 16; Pitman, *supra* note 24, at 23.

[30] *Unclaimed Property Act Summary*, *supra* note 16.

[31] Pitman, Schiefelbein, & Starr, *supra* note 24, at 23.

[32] Ethan D. Millar et al., *Unclaimed Property: Development of State Statutory Law*, Tax Mgmt. Port. (BNA) 1600.02-3rd (2018).

[33] *See* Millar et al., *supra* note 32.

[34] *See* Millar et al., *supra* note 32.

[35] *See* Millar et al., *supra* note 32.

[36] *See* Millar et al., *supra* note 32; Diane Green-Kelly, *An Ancient Concept Creating Modern Liabilities*, 32 Franchise L.J. 41 (2012).

[37] Millar et al., *supra* note 32 (listing Connecticut, Delaware, Kentucky, Massachusetts, New York, Ohio, Pennsylvania, and Texas, though noting that some have incorporated certain UUPA provisions in their statutes).

[38] Green-Kelly, *supra* note 36, at 41.

[39] Millar et al., *supra* note 32.

Article. Several states have considered RUUPA bills and, according to the ULC, Tennessee, Utah and Kentucky have adopted some form of RUUPA.[40]

III. Derivative Rights Doctrine

A fundamental principle of unclaimed property law is the "derivative rights doctrine," which provides that the state's right to claim unclaimed property is derivative of the owner's right to the property. In other words, the state steps into the shoes of the owner and can claim from the holder only that which the owner was entitled. Thus, under a pure application of the doctrine, where an owner has no right to particular property, the state will derivatively have no ability to escheat the property as unclaimed property.

Several courts have recognized the applicability of the derivative rights doctrine. For example, in *Kane v. Insurance Co. of North America*,[41] the Commonwealth Court of Pennsylvania affirmed the trial court's ruling that the state had no right to escheat certain property because the funds were not unqualified because the owners' and the state's rights are derivative of, and thus no larger than, the owners' rights. The court held that the state's "rights in an escheat proceeding are derivative . . . . [The state] can claim no more than the interest of the unknown or absentee owner."[42]

Similarly, in *Insurance Co. of North America v. Knight*,[43] the Illinois Appellate Court affirmed a lower court decision that an insurer had no obligation to report certain checks, drafts and credit memoranda to the state as unclaimed property. The court noted that "the rights of the State are derivative from the rights of the owner, and . . . the State has no greater right than that of the payee owner."[44]

The derivative rights doctrine has been widely adopted among California courts, including in *Bank of America National Trust & Savings Ass'n v. Cranston*, in which the Court of Appeal held that "[t]he Controller's rights under the [California Unclaimed Property Law] are derivative.[45] [The Comptroller] succeeds, subject to the act's provisions, to whatever rights the owners of the abandoned property may have."[46] The appellate court reaffirmed this proclamation in *Blue Cross of Northern California v. Cory*, stating that "the Controller's rights under the [Unclaimed Property Law] are 'derivative,' and that [the Comptroller] accordingly succeeds to whatever rights the owner of

[40] *See Legislation*, Unif. Law Comm'n, last accessed Aug. 6, 2018, http://www.uniformlaws.org/Legislation.aspx (listing RUUPA bills in District of Columbia, Kentucky, Maine, Minnesota, Nebraska, Vermont, and Washington).

[41] Kane v. Ins. Co. of N. Am., 392 A.2d 325 (Pa. Commw. Ct. 1978).

[42] *Id.* at 329 (internal citations omitted).

[43] Ins. Co. of N. Am. v. Knight, 291 N.E.2d 40 (Ill. App. Ct. 1972), *appeal dismissed*, 414 U.S. 804 (1973).

[44] *Id.* at 44.

[45] Bank of Am. Nat'l Tr. & Sav. Ass'n v. Cranston, 252 Cal.App.2d 208, 211 (Ct. App. 1967).

[46] *Id.*

unclaimed property may have and no more."[47] New Jersey courts have also upheld the viability of the doctrine on several occasions. In particular, in *State v. United States Steel Corp.*, the Supreme Court of New Jersey noted:

> Limitations operate not against the State per se, but against the basic claim of the unknown owner. If, by virtue of limitations, the owner can obtain nothing, the State is under like disability. This is the derivative consequence, long recognized in the law of escheat. The right of action to escheat or to obtain custody of unclaimed property is not derivative; but what may be obtained by exercise of the right is dependent upon the integrity of the underlying obligation.[48]

In *State v. Elizabethtown Water Co.*,[49] the Supreme Court of New Jersey affirmed the appellate court's ruling that the state had no right to escheat funds resulting from unrefunded deposits for water utility main construction based on the contractual rights between the holder—the water utility—and the putative owners—the developers—which allowed the utility to keep any unrefunded deposits and placed the burden of the speculative risks on the developers. The court relied on the derivative rights doctrine, noting that "the State's claims are nonetheless derivative and certainly no broader than the developers' claims."[50] In another New Jersey case, *State v. Sperry & Hutchinson Co.*,[51] the Supreme Court of New Jersey held that the state had no right to escheat the value of unredeemed trading stamps when the contractual terms required a minimum quantity for redemption, noting that the "State's rights are no greater than that of each stamp holder" and are "entirely derivative."[52]

Most recently, in *Temple-Inland, Inc. v. Cook*, the U.S. District Court for the District of Delaware stated:

> It is true that, '[u]nlike taxation (where a state holds direct legal authority to collect, retain, and spend tax revenue for purposes of funding governmental operations), a state's authority to receive and retain unclaimed property is derived from the owner's rights in that property.' Consistent with the principle that states have no greater rights than the owner, the U.S. Supreme Court has stated that the first step in determining which state may escheat unclaimed property is determining the precise relationship between the holder and owner. Thus, it seems appropriate that [the state has] the burden of proving that the property is in fact unclaimed.[53]

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[47] Blue Cross of N. Cal v. Cory, 120 Cal.App.3d 723, 737 (Ct. App. 1981).

[48] State v. U.S. Steel Corp., 126 A.2d 168, 173 (N.J. 1956) (citations omitted).

[49] State v. Elizabethtown Water Co., 191 A.2d 457 (N.J. 1963).

[50] *Id.* at 458.

[51] State v. Sperry & Hutchinson Co., 153 A.2d 691 (N.J. Super. App. Div. 1959), *aff'd per curiam*, 157 A.2d 505 (N.J. 1960).

[52] *Id.* at 699-700.

[53] Temple-Inland, Inc. v. Cook, 192 F. Supp. 3d 527, 545 (D. Del. 2016) (footnote ommitted) (citations ommitted).

However, as a general matter, the derivative rights doctrine is not expressly incorporated into states' unclaimed property statutes, other than perhaps in the context of the definition of "intangible property" to the extent a particular statute requires the property to be a "fixed and certain interest."[54] And states have become increasingly resistant to the notion that their ability to enforce their laws is somehow constrained by this doctrine. Thus, over the years, the derivative rights doctrine has been diluted somewhat and its role in the administration of unclaimed property laws has been minimized. For example:

- Many state unclaimed property laws include a so-called "anti-limitations" provision, which essentially provide that even if a purported owner was time-barred by law or by contract from recovering the property at issue, the holder would still have to report and remit the property to the state.[55] Arguably, this results in some enlargement of the states' property interest compared to the owners', because the holder must remit funds to the state as unclaimed property that the owner would have no right to claim directly from the holder.
- Twenty-seven states currently require the escheatment of gift certificates and gift cards, even if such instruments are not redeemable for cash and may only be redeemed for merchandise or services.[56] A more complete discussion of this issue is addressed *infra* Part IV. The fact that a state can require a holder to remit cash with respect to an unredeemed gift certificate, which the owner could not obtain, clearly reflects an enlargement of the state's rights vis a vis the owner's.
- State unclaimed property laws that are based on either the 1981 UUPA or 1995 UUPA include a provision requiring property to be escheated even if the owner has not demanded the property from the holder or otherwise satisfied conditions precedent to being entitled to the property.[57] These provisions undercut the derivative rights doctrine by requiring that a state need not comply with certain contractual terms required of owners to escheat unclaimed property.

In its role in shaping RUUPA, the National Association of Unclaimed Property Administrators submitted a position paper to the ULC, which stated:

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[54] *Id.*

[55] *See, e.g.*, Unif. Unclaimed Prop. Act § 19 (Unif. Law Comm'n 1995) [hereinafter UUPA] ("The expiration . . . of a period of limitation on the owner's right to receive or recover property, whether specified by contract, statute, or court order, does not preclude the property from being presumed abandoned or affect a duty to file a report or to pay or deliver or transfer property" to the state as required by law."). The 1981 version of the Act contains a very similar provision.

[56] A subset of these 27 states would only escheat gift certificates or gift cards that expire.

[57] *See* Unif. Unclaimed Prop. Act § 2(b) (Unif. Law Comm'n 1981, superseded 1995) [hereinafter 1981 UUPA] ("Property is payable or distributable for the purpose of this Act notwithstanding the owner's failure to make demand or to present any instrument or document required to receive payment."). The 1995 version of UUPA contains a very similar provision.

> Enactment of the holder advocates' notion of derivative rights would probably result in emasculation of State unclaimed property programs. Because a holder can easily invent some business purpose for any restriction on its obligation to the owners, surely all would do so. Any holder issuing a payment instrument or credit of any form—check, rebate, refund, traveler check, money order, stored value card, credit balance—would require that the instrument or credit be cashed or used within a time period fixed so that the holder can confiscate the funds.[58]

This clearly demonstrates the states' collective skepticism to the concept of derivative rights.

Despite the efforts of various holder organizations, RUUPA does not reflect a significant upgrade in terms of recognition and incorporation of the derivative rights doctrine as compared with the 1981 UUPA and 1995 UUPA. Indeed, RUUPA carries forward the same anti-limitations provisions and non-presentment (*i.e.*, demand for payment) requirements found in the prior UUPAs. For example, section 610 of RUUPA provides:

> Expiration, before, on, or after the effective date of this [Act], of a period of limitation on an owner's right to receive or recover property, whether specified by contract, statute, or court order, does not prevent the property from being presumed abandoned or affect the duty of a holder under this [Act] to file a report or pay or deliver property to the administrator.[59]

In addition, RUUPA provides states with the option of either exempting or escheating gift cards (even if such cards do not expire) and in-store credits for returned merchandise.[60] Moreover, RUUPA continues to allow states to escheat property in the absence of presentment. Indeed, the language in section 405 is identical to the language of the analogous provisions in the 1981 UUPA and 1995 UUPA.[61]

Accordingly, as more states adopt RUUPA, the role of the derivative rights doctrine in the administration of state unclaimed property laws will continue to shrink, particularly when combined with the increasing skepticism by states toward the validity of the doctrine. The result of this, in the Authors' view, is that unclaimed property laws will evolve from laws that are primarily intended to reunite property with its rightful owner to mechanisms designed to enrich state revenues. This would appear to be contrary to the original purpose of custodial escheat laws.

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[58] *See* Memorandum from Unif. Unclaimed Prop. Act Revision Comm., Nat'l Ass'n of Unclaimed Prop. Admins., The Derivative Rights Doctrine Under Unclaimed Property Law, The Holder Advocates' Notion of that Doctrine, and Implications for Unclaimed Property Administration (May 29, 2014), https://www.unclaimed.org/uploads/resources/256/naupa-derivative-rights-doctrine-whitepaper.pdf.

[59] *See* Memorandum, Nat'l Ass'n of Unclaimed Prop. Admins., *supra* note 58.

[60] *See* Memorandum, Nat'l Ass'n of Unclaimed Prop. Admins., *supra* note 58.

[61] *See* RUUPA § 405 ("Property is reportable and payable or deliverable under this [Act] even if the owner fails to make demand or present an instrument or document otherwise required to obtain payment.").

At a minimum, as discussed in more detail in Part IV, in order to address these deficiencies, states adopting RUUPA should opt to exempt both gift cards and in-store merchandise credits. This would preserve the notion that non-cash obligations should not be required to be reported and remitted as unclaimed property. States could also consider omitting language from the anti-limitations provision that would extend the requirements to contractual limitations provisions. The effect of this would be to respect the effect of an otherwise valid contract between two consenting parties, impacting the ability of each party to recover amounts from the other. Finally, in enforcing their unclaimed property laws, states should respect the requirement that property interests be "fixed and certain," which should represent meaningful limitations on a state's ability to escheat property.[62]

IV. Gift Cards and Similar Instruments

Gift cards have become an increasingly popular way for consumers to make purchases over the past 20 years. Most often, gift cards take the form of a plastic card that has been pre-loaded for a certain dollar amount, although retailers have expanded their e-gift card programs over the past years. The gift card may be a "retail gift card"—often referred to as a "closed-loop" gift card—that can only be redeemed by a specific retailer or a "bank gift card" that carries the logo of American Express, Visa, or another bank that can be used to purchase goods or services virtually anywhere—often referred to as an "open-loop" gift card. A typical characteristic of most gift cards is that it cannot be redeemed for or otherwise converted into cash.

Each year, it is estimated that consumers spend approximately $130 billion on gift cards, with approximately $1 billion going unspent, which underscores the potential impact gift cards have on state budgets if subject to escheat under state unclaimed property law.[63] When the value of such gift cards has not been fully utilized after a specific period of time, the remaining unused portion may be treated as having been "abandoned" and thus subject to the unclaimed property rules of one or more states.

The Comments to RUUPA (Comments) note that thirty-six states currently provide an exemption for gift cards from their unclaimed property statutes.[64] Some of the states limit the exemption to gift cards that have no

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[62] *See id.* § 102(24).

[63] Kari Paul, *$1 Billion in Gift Cards Go Unused Every Year — Here's How to Avoid That*, Market Watch, last accessed Jan. 1, 2018, https://www.marketwatch.com/story/1-billion-in-gift-cards-go-unused-every-year-heres-how-to-avoid-that-2016-12-30.

[64] *See* RUUPA prefatory cmt. p. 22.

expiration date,[65] while others provide an outright exemption for all gift cards without regard to any expiration date.[66] Other states provide an exemption based on the unredeemed value remaining on the card.[67]

According to the Comments, the fourteen states, plus the District of Columbia, that do not exempt gift cards find that funds from lost or forgotten gift cards probably never will be claimed by the owners because the owner's name and address is rarely discernable (although that may be changing the more companies transition to different models for tracking owner activity and interaction).[68] The states reason that if an exemption were provided, the holder of the gift card may receive an unjust windfall.[69] In that case, the states conclude that they, not the holder, should benefit from any windfall of funds from unclaimed gift cards.[70]

RUUPA continues to give states the flexibility to exempt or not exempt gift cards from their unclaimed property laws. This is accomplished by bracketing the relevant provisions, along with instructions in the Comments to either delete the brackets or pertinent language in its entirety, depending on whether exemption is desired. For example, RUUPA section 101(24)(C) provides that "property" does not include "[a gift card]."[71] States that wish to exempt gift cards would remove the brackets, while those wishing to include gift cards would delete the entire provision.[72]

For states that provide no exemption for gift cards, RUUPA section 102(11) defines a "gift card" as:

> (A) a stored-value card: (i) the value of which does not expire; (ii) that may be decreased in value only by redemption for merchandise, goods, or services; and (iii) that, unless required by law, may not be redeemed for or converted into money or otherwise monetized by the issuer; and

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[65] *See e.g.*, Cal. Civ. Proc. Code § 1520.5 (West 2018); other states include HI, ID, IL, IA, NE, NV, NC, PA, RI, SD, TN, TX, and WA. It is important to note that issuers are already constrained on the imposition of expiration by federal law governing gift cards. The Credit Card Accountability Responsibility and Disclosure Act of 2009 provides that (i) money on a gift card cannot expire for at least five years from the date the card was purchased, or from the date additional money was loaded onto the card; (ii) the card must clearly disclose its expiration date; and (iii) inactivity fees can be charged only after the card hasn't been used for at least one year. *See* Credit Card Accountability and Responsibility Act of 2009 (Credit CARD Act), Pub. L. No. 111-24, § 401, 123 Stat. 1734 (codified as amended at 15 U.S.C. § 1693/-1(b) to (c) (2018)); 12 C.F.R. § 205.20 (2018).

[66] *See, e.g.*, Ala. Code § 35-12-73(b)(1) (2018); other states include AZ, AR, CT, FL, IN, MD, MA, MI, MN, NH, OH, UT, VT, and VA.

[67] *See, e.g.*, N.H. Rev. Stat. Ann. § 471-C:16 (2018); other states include ID and MI.

[68] *See* RUUPA prefatory cmt. p. 10.

[69] *See id.* prefatory cmt. p. 9.

[70] *See id.* prefatory cmt. p. 10.

[71] *See id.* § 102(24)(C).

[72] Other instances where bracketed language must be modified, or deleted, include RUUPA section 201(13) ("When Property Presumed Abandoned") and RUUPA section 206(a) ("When Store-Value Card Presumed Abandoned").

(B) includes a prepaid commercial mobile radio service, as defined in 47 C.F.R. 20.3[, as amended].[73]

Under RUUPA section 210, a gift card is presumed abandoned if it is unclaimed by the apparent owner five years after the later of the date of purchase or its most recent use.[74]

In general, RUUPA's definition for gift cards and the five year presumption for abandonment are not controversial. However, RUPPA does provide that a gift card's value can only be decreased for redemption of merchandise, goods, or services.

The Comments provide that RUUPA does not take a position as to whether any unredeemed balances (or specific dollar amounts on such unredeemed balances) should be covered by RUUPA.[75] The lack of a formal position in this regard may be problematic for states that base their exemption on specific dollar amounts remaining on the gift card. Also, RUUPA does not provide any reduction in the amount that must be reported, unlike the 1995 UUPA, which provided only 60% of the unredeemed value was reportable due to the constitutional considerations addressed below.[76]

More fundamentally, RUUPA's failure to take a position on an exemption for gift cards and in-store merchandise credits that are not redeemable for cash is a failure to recognize the derivative rights principle insofar as it would change the underlying debtor-creditor relationship, rather than defer to it. RUUPA's failure to do so is even more surprising given that the majority of states already exempt gift cards in some fashion.

In addition, RUUPA created additional constitutional concerns by providing that if a state does elect to escheat gift cards, the amount escheatable is cash equal to the unredeemed gift card balance, rather than cash equal to 60% of the unredeemed card balance, which was the rule adopted in the 1995 UUPA to recognize that merchandise and services are sold by retailers at a profit, and that escheatment of the full 100% of the card balance would deprive the retailer of its anticipated profits.[77] RUUPA's backsliding in this regard should be noted to any state that is considering adopting RUUPA.

V. Third-Priority Rule for when the Transaction "Occurred in the State"

Section 305 of RUUPA retains the "transactional rule" or "third-priority rule" of the 1981 and 1995 UUPA allowing the state unclaimed property administrator to take custody of an item of property presumed abandoned if:

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[73] RUPPA § 102(11). Gift cards are a subset of "store-value cards." RUUPA defines a "stored-value card" as a record evidencing a promise made for consideration by the seller or issuer of the record that goods, services, or money will be provided to the owner of the record to the value or amount shown in the record. *Id.*

[74] *Id.* § 210.

[75] *Id.* § 102.

[76] See *id.*; Serv. Merch. Co. v. Adams, No. 97-2782-III, 2001 WL 34384462, at *6-7 (Tenn. Ch. Ct. June 29, 2001).

[77] RUUPA § 102.

(1) the transaction involving the property occurred in the state (hereinafter referred to as the "transaction state"), (2) the last known address of the apparent owner of the property item is either unknown or in another state that does not provide for the custodial taking of the property item, and (3) the holder of the property item is domiciled (*i.e.*, incorporated in or organized under the laws of) in another state that does not provide for the custodial taking of the property item, all subject to the caveat that the owner's state of last known address and the holder's state of domicile do not specifically exempt the property item under their unclaimed property laws.[78]

Requiring the transaction state to respect the exemption(s) of the higher-priority state of last known address of the owner or the holder's state of corporate domicile is a clear improvement over the third-priority rule of the 1981 and 1995 Uniform Acts. The fact remains, however, that this third-priority rule has been repeatedly considered and rejected by the United States Supreme Court and the lower federal courts as being inconsistent with the Supreme Court's priority rules for determining which state is entitled to claim custody of unclaimed property items.[79] Moreover, with all 50 states now having adopted unclaimed property laws, the transaction state would only be in a position to claim custody of a property item pursuant to the third-priority rule if the holder's state of corporate domicile provides an exemption for the property item, yet section 305 does not allow the transaction state to claim custody of a property item that is exempted by that higher-priority state. This renders section 305 superfluous. Accordingly, a state legislature considering adoption of RUUPA should consider omitting section 305 from its RUUPA legislation.

VI. The Development of the Supreme Court's Priority Rules

In the late 1940s and early 1950s, the Supreme Court was presented with several cases in which states were attempting to claim custody of unclaimed property items from a holder based on the state's claim that it had jurisdiction under the Due Process Clause to apply its unclaimed property laws to the holder and the property items were presumed abandoned under the state's unclaimed property law. In *Connecticut Mutual Life Insurance Co. v. Moore*, the Supreme Court upheld New York's right to take custody of unclaimed proceeds of insurance policies that the defendant insurance companies had issued on the lives of New York residents.[80] Applying a due process "contacts" analysis, the Supreme Court held that, even though none of the defendant insurance companies were incorporated in New York, the state nevertheless had jurisdiction to require the insurance companies to report the unclaimed insurance proceeds to New York because the insurance companies were doing

[78] *See* 1981 UUPA § 3(6); UUPA § 4(6).
[79] *See* 1981 UUPA § 3(6); UUPA § 4(6).
[80] Conn. Mut. Life Ins. Co. v. Moore, 333 U.S. 541 (1948).

business in New York and the insureds resided in New York.[81] The Supreme Court noted that the question of whether another state would also have sufficient due process contacts to be able to claim custody of the same property items from the insurance companies was not before the Court.[82]

Three years later, in *Standard Oil Co. v. New Jersey*, the Supreme Court allowed New Jersey to take custody of unclaimed dividends and shares of stock from Standard Oil Company on the grounds that this holder was incorporated in New Jersey, even though Standard Oil's books and records indicated that many of the owners of these unclaimed property items resided in states other than New Jersey.[83] The Supreme Court again upheld the claimant state's right to take custody of the unclaimed property from the holder because the holder was subject to the due process jurisdiction of the claimant state, explaining, "We see no reason to doubt that, where the debtor and creditor are within the jurisdiction of a court, that court has constitutional power to deal with the debt."[84] The Supreme Court ruled only upon the constitutionality of New Jersey's claim to escheat the property at issue, emphasizing that "the claim of no other state to this property is before us and, of course, determination of any right of the claimant state against New Jersey for the property escheated by New Jersey must await presentation here."[85]

However, in *Western Union Telegraph Co. v. Pennsylvania*, the Supreme Court did not allow Pennsylvania to claim custody of unclaimed money order funds from Western Union because Pennsylvania would not have been able to protect Western Union from the double liability that would result if and when New York, Western Union's state of incorporation (and possibly other states), laid claim to the same money order funds.[86] Again, the issue of which state possessed the superior right to claim the money order funds in the possession of Western Union was not before the Court.

In the seminal case of *Texas v. New Jersey*,[87] the Supreme Court was finally presented with the question of which state had the superior right to claim custody of items of intangible property from the holder. Unlike earlier cases, this original jurisdiction action dealt not with whether the holder had sufficient contacts with a state to make its property rights subject to the jurisdiction of its courts, but with the very different problem of deciding which state's claim to escheat unclaimed property from the holder is superior to all others.[88]

New Jersey was claiming the property items in its capacity as the state of incorporation of the holder, Sun Oil Company.[89] Pennsylvania contended

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[81] *Id*. at 548.
[82] *Id.*
[83] Standard Oil Co. v. New Jersey, 341 U.S. 428 (1951).
[84] *Id*. at 439.
[85] *Id.*
[86] W. Union Tel. Co. v. Pennsylvania, 368 U.S. 71, 76-77 (1961).
[87] Texas v. New Jersey, 379 U.S. 674 (1965).
[88] *Id.* at 678-79.
[89] *Id.* at 676.

that it should be allowed to claim custody of all of the unclaimed property on the books of Sun Oil because it was the state of commercial domicile of Sun Oil.[90] Florida and Texas claimed custody of certain property items on the grounds that their owners resided in that state, or in the case of Texas, that the property items were recorded on the books and records of two Sun Oil offices located in Texas.[91] Meanwhile, Illinois proposed a transaction rule pursuant to which "jurisdiction to escheat should depend on the laws of the state in which the indebtedness was created."[92]

The Supreme Court recognized in *Texas v. New Jersey* that the Court finally needed to create a straightforward set of rules that states would follow when they claimed custody of property items from holders. The Court explained:

> Since the States separately are without constitutional power to provide a rule to settle this interstate controversy and since there is no applicable federal statute, it becomes our responsibility in the exercise of our original jurisdiction to adopt a rule which will settle the question of which State will be allowed to escheat the intangible property.[93]

The Supreme Court also emphasized the importance of establishing priority rules that would be easy for holders and the states to administer. For this reason, the Court rejected both Pennsylvania's suggestion that the unclaimed property at issue in *Texas v. New Jersey* should be subject to escheat by the state of the principal place of business of the holder, *and the transaction rule proposed by Illinois*, because the Court concluded:

> [A]pplication of the rule Pennsylvania suggests would raise in every case the sometimes difficult question of where a company's 'main office' or 'principal place of business' or whatever it might be designated is located. *Similar uncertainties would result if we were to attempt in each case to determine the State in which the debt was created and allow it to escheat.* Any rule leaving so much for decision on a case-by-case basis should not be adopted unless none is available which is more certain and yet still fair.[94]

Under the two priority rules that the Supreme Court adopted in its *Texas v. New Jersey* decision, unclaimed property escheats, first, to the state of the last known address of the apparent owner of the property, as shown in the holder's books and records.[95] The Supreme Court explained:

> Adoption of such a rule involves a factual issue simple and easy to resolve, and leaves no legal issue to be decided . . . . And by using a standard of last known address, rather than technical legal concepts of residence and domicile, administration and application of escheat laws should be simplified.[96]

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[90] *Id.*
[91] *Id.* at 675-76.
[92] *Id.* at 676 n.6.
[93] *Id.* at 677.
[94] *Id.* at 680 (emphasis added).
[95] *Id.* at 680-81.
[96] *Id.* at 681.

The Supreme Court went on to provide a secondary priority rule that is applicable to "property owed persons (1) as to whom there is no record of any address at all, or (2) whose last known address is in a State which does not provide for escheat of the property owed them."[97] The Supreme Court decided that the holder's state of corporate domicile (*i.e.*, its state of incorporation) is allowed to take custody of the property under this secondary priority rule, with the caveat that the state of last known address of the owner of the property item can subsequently claim the property item from the state of the holder's corporate domicile "upon proof that the last known address of the creditor was within its borders" or "if and when its law made provision for escheat of such property."[98] When the *Texas v. New Jersey* case was decided in 1965, a significant number of states had not yet enacted unclaimed property laws.[99]

In *Pennsylvania v. New York*, Pennsylvania asked the Supreme Court to create a special priority rule for unclaimed money order funds.[100] Because money order issuers like Western Union did not regularly record where the sender or payee of the money order resided, there was no state of last known address of the owner in a position to claim custody of the money order funds from the holder pursuant to the primary priority rule of *Texas v. New Jersey*. Pennsylvania urged the Court to prevent a "windfall" to New York, the state of incorporation of the holder Western Union, by giving the first priority claim to the state where the money order had been purchased (and where the sender of the money order presumably resided).[101] This transactional rule would authorize the state of purchase to claim custody of money order funds ahead of the state of incorporation of the holder.

The Court declined Pennsylvania's request for the creation of a special exception to its two priority rules for money orders, in part because of the concerns expressed by the Special Master that "the place-of-purchase . . . rule[] might permit intangible property rights to be 'cut off or adversely affected by . . . a forum having no continuing relationship to any of the parties'" or to the transaction.[102] But beyond endorsing this concern that a transaction state might have insufficient ties to the holder and the owner of the money order funds to justify giving the transaction state the right to claim custody of the funds, the Court concluded:

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[97] *Id.* at 682.

[98] *Id.*

[99] The Prefatory Note to the 1966 revisions to the 1954 UUPA states that when the 1954 UUPA was being drafted "only ten states had adopted really comprehensive legislation covering the entire field of unclaimed property." Willoughby A. Colby, *The 1954 Uniform and Model Acts: A Summary and Analysis*, 41 A.B.A. J. 39, 39 (1955). In addition, the Supreme Court noted in *Western Union Telegraph Co. v. Pennsylvania* that several states were then in the process of enacting or expanding the scope of their unclaimed property laws. 368 U.S. 71, 76-77 (1961).

[100] 407 U.S. 206 (1972).

[101] *Id.* at 210-11.

[102] *Id.* at 213.

> [T]o vary the application of the *Texas* rule according to the adequacy of the debtor's records would require this Court to do precisely what we said should be avoided—that is, 'to decide each escheat case on the basis of its particular facts or to devise new rules of law to apply to ever developing new categories of facts.'[103]

The Supreme Court did give Pennsylvania and the other plaintiff states the opportunity to research Western Union's archived money order transaction records to prove up that the owners of particular unclaimed money order funds had a last known address in the plaintiff state. But absent such evidence that the owner resided in the plaintiff state, New York, as the state of corporate domicile of the holder, Western Union, would be allowed to take custody of the unclaimed money order funds pursuant to the secondary priority rule of *Texas v New Jersey*.[104]

In *Delaware v. New York*, the Supreme Court was asked to clarify how the secondary priority rule of *Texas v. New Jersey* should be applied to unclaimed securities distributions held by intermediary banks, brokers and depositories, as "record owners" of the securities, for the beneficial owners of those securities who could not be identified or located in the financial intermediary's records.[105] Between 1985 and 1989, New York had asserted an aggressive transactional rule claim to $360 million of unclaimed securities distributions held by financial intermediaries transacting business in New York, without regard to either the state of last known address of the beneficial owner or the financial intermediary's state of incorporation.[106] Delaware filed an original jurisdiction action against New York in the Supreme Court, alleging that New York's transactional-rule claim to those unclaimed securities distributions was contrary to the priority rules of *Texas v. New Jersey*.[107] The Supreme Court ultimately held that unless a state was able to prove that specific unclaimed distributions were owed to specific beneficial owners with last known residences in that state, the secondary priority rule of *Texas v. New Jersey* would award custody of the unclaimed securities distributions to the state of incorporation (most likely Delaware) of the financial intermediary holding the unclaimed distributions.[108] The Court flatly rejected New York's position that

[103] *Id*. at 215 (citation omitted).

[104] In response to the holding of *Pennsylvania v. New York*, in 1972 Congress enacted a special set of federal statutory priority rules for unclaimed sums payable on a "money order, traveler's check, or other similar written instrument (other than a third party bank check)." 12 U.S.C. §§ 2501-2503 (2018). Under these federal priority rules, such unclaimed funds are reportable, first, to the state in which the money order or traveler's check was purchased. If the books and records of the holder do not indicate the state of purchase (or the laws of that state do not provide for the escheat or custodial taking of the money order or traveler's check funds), then the unclaimed funds are reportable to the state of principal place of business of the holder. § 2501.

[105] Delaware v. New York, 507 U.S. 490 (1993).

[106] *Id.* at 496.

[107] *Id.* at 496-97.

[108] *Id*. at 507.

because the transactions involving the unclaimed securities distributions had occurred in New York, that state should be allowed to claim custody of the funds. The Court pointedly noted that its two priority rules "arise from our 'authority and duty to determine for [ourselves] all questions that pertain' to a controversy between States . . . and no State may supersede them by purporting to prescribe a different priority under state law."[109]

VII. More Recently, the Third Circuit Squarely Rejected the Third-Priority Rule

For more than ten years, New Jersey common law provided that unclaimed gift certificates were not escheatable to New Jersey pursuant to its Unclaimed Property Law because gift certificates are typically not redeemable for cash and the state's Unclaimed Property Law was not intended to "impose an obligation [on the holder] different from the obligation undertaken to the original owner" of the gift certificates.[110] In 2010, the New Jersey General Legislature overturned this common law rule by adding a provision to the state's Unclaimed Property Law that treated gift certificates, gift cards and stored value cards (collectively, SVCs) as unclaimed property after a relatively short two-year dormancy period.[111] This legislation, commonly referred to as "Chapter 25," included a "place-of-purchase" priority rule providing that if the issuer of an SVC did not maintain record of the name and address (or at least the zip code) of the purchaser or owner of the SVC, the address of the place where the SVC was purchased or issued would be assumed to be the address of the purchaser or owner.[112] By presuming that the state of last known address of the owner of an SVC purchased in New Jersey was in New Jersey, this transaction rule was intended to allow New Jersey to take custody of the unclaimed SVC funds pursuant to the first priority rule of *Texas v. New Jersey*.

The New Jersey State Treasurer provided administrative guidance on September 23, 2010, to issuers of SVCs that if the issuer had its corporate domicile in a state other than New Jersey *and* that state exempted SVCs under its unclaimed property laws, any unredeemed balances on SVCs sold in New Jersey prior to September 23, 2010, for which the issuer had not recorded names and addresses (or at least zip codes) of the purchasers or owners of

[109] *Id.* at 500 (quoting Kentucky v. Indiana, 281 U.S. 163, 176 (1930)).

[110] *In re* Nov. 8, 1996, Determination of N.J., Dept. of Treas., Unclaimed Prop. Office, 706 A.2d 1177, 1180 (N.J. Super. Ct. App. Div. 1998).

[111] 2010 N.J. Laws 3002 (codified at N.J. Stat. Ann. § 46:30B-42.1 (West 2010)).

[112] N.J. Stat. Ann. § 46:30B-42.1(c) (West 2010), *prior version invalidated by* Am. Exp. Travel Related Servs. Co. v. Sidamon-Eristoff, 755 F. Supp. 2d 556, 564 (D.N.J. 2010), *aff'd sub nom*, N.J. Retail Merchs. Ass'n v. Sidamon-Eristoff, 669 F.3d 374 (3d Cir. 2012).

the SVCs, would be reportable to New Jersey, pursuant to the existing third-priority rule in the New Jersey Unclaimed Property Law.[113]

In 2012, in *New Jersey Retail Merchants Ass'n v. Sidamon-Eristoff*, the U.S. Court of Appeals for the Third Circuit affirmed the district court's holding that both the place-of-purchase priority rule in Chapter 25 and the third-priority rule in the New Jersey Unclaimed Property Law were preempted by the Supreme Court's *Texas v. New Jersey* priority rules.[114] The Third Circuit cited the Supreme Court's *Pennsylvania v. New York* opinion for the proposition that "New Jersey, as the state in which the SVC was purchased, does not have sufficient connection with any of the parties to the transaction to claim a right to escheat the abandoned property."[115] The Third Circuit held that the place-of-purchase priority rule in Chapter 25 was preempted by the secondary priority rule of *Texas v. New Jersey*, because the plaintiff SVC issuers could not escheat the unredeemed balance on an SVC purchased in New Jersey to both New Jersey, pursuant the place-of-purchase rule, and the issuer's state of corporate domicile, pursuant to the secondary priority rule of *Texas v. New Jersey*.[116] The Third Circuit also rejected the Treasurer's attempt to opportunistically claim custody of unredeemed balances on pre-2012 SVCs exempted by the unclaimed property laws of the SVC issuer's state of corporate domicile via the third-priority rule in the New Jersey Unclaimed Property Law because this would negate the exemption of the state having a superior right to escheat the SVC balances under the secondary priority rule of *Texas v. New Jersey,* as reaffirmed in *Delaware v. New York*. The Third Circuit explained its reasoning:

> As the *Delaware* court recognized, 'the secondary rule protects the interests of the debtor's [s]tate as *sovereign* over the remaining party to the underlying transaction.' 507 U.S. at 504 (emphasis added). The Supreme Court has long recognized that the sovereign maintains authority over abandoned property, including the right to escheat the property. *See Texas*, 39 U.S. at 675. The ability to escheat necessarily entails the ability not to escheat. To say otherwise could force a state to escheat against its will, leading to a result inconsistent with the basic principle of sovereignty. . . .
>
> But the place-of-purchase presumption, executed in accordance with the Treasury Guidance [really the third-priority rule], allows New Jersey to infringe on the sovereign authority of other states. Even when states decide not to exercise custodial escheat with the intent of allowing the holders to maintain custody of the property, the place-of-purchase presumption gives New Jersey the right to make the holder, SVC Issuers in this case, turn over

[113] Office of N.J. State Treasurer, Treasury Announcement: Guidance on Implementation and Notice of Exemption from Certain Provisions of L. 2010, c. 25 (Sept. 23, 2010), at 3.

[114] N.J. Retail Merchs. Ass'n v. Sidamon-Eristoff, 669 F.3d 374 (3d Cir. 2012), *cert. denied*, 568 U.S. 978 (2012).

[115] *Id.* at 394-95.

[116] *Id.* at 392-93.

> the property to the State. When fashioning the priority rules, the Supreme Court did not intend such a result, which would give states the right to override other state's sovereign decisions regarding the exercise of custodial escheat[s].[117]

The closest thing there is to a case supporting a state third-priority rule claim against a holder is *Sperry & Hutchinson Co. v. O'Connor*, and the reported Pennsylvania Supreme Court decision in that case did not reach the validity of the state claim.[118] In light of the Supreme Court and Third Circuit cases discussed earlier, the Uniform Law Commission (ULC) drafting committee should have eliminated the third-priority rule from RUUPA. The Third Circuit correctly held in *New Jersey Retail Merchants Ass'n* that the third-priority rule is preempted by the *Texas v. New Jersey* priority rules and that to allow the transaction state to take custody of property that has been exempted by the higher-priority state of corporate domicile of the holder would negate the exemption of that state, infringing on its sovereign right to enact the exemption.[119] Moreover, section 305 of RUUPA expressly prohibits the transaction state from taking custody of a property item pursuant to the third-priority rule if the holder's state of corporate domicile has a specific exemption applicable to the property item.[120] With the third-priority rule being rendered superfluous, it should be omitted from RUUPA legislation that states may be considering adopting.

VIII. Treatment of Presumed-Abandoned Securities and Investment Assets

RUUPA has implemented several policies with respect to securities and accounts that represent significant improvements over the practices of a number of states, and which have the goal of providing greater protection to owners of investment assets. These policies relate to two specific areas impacting owners of securities and financial assets held in a security account held by a registered broker–dealer, as well as tax-deferred retirement accounts[121] (although this type of account is separately addressed in RUUPA due to their unique dormancy considerations), namely: (1) dormancy standard and dormancy trigger (*i.e.*, the event the commences running of the dormancy

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[117] *Id.* at 395.

[118] *See* Sperry & Hutchinson Co. v. O'Connor, 412 A.2d 539 (Pa. 1980).

[119] *N.J. Retail*, 669 F.3d 374, 395.

[120] RUUPA § 305

[121] The RUUPA Comment on section 202, Tax Deferred Retirement Accounts, states:

> The 1995 UUPA provided a three year dormancy period for unpaid distributions from retirement accounts. Section 202 retains the dormancy period of three years, but clarifies when the dormancy period is triggered for such accounts based on return of first class United States mailings, date an owner reaches the age of mandatory distribution or confirmation of apparent owner death.

RUUPA § 202 cmt.

period); and (2) restrictions on a custodial state's right to liquidate securities or accounts holding securities.

A. *Dormancy Standard and Trigger*

With regard to the dormancy standard and the trigger event that commences a dormancy clock to run, the question that occupied RUUPA's drafting committee was whether it is appropriate to assess the dormancy of a security or investment account based solely on an owner's level of contact or activity with respect to the security or account. Investment industry professionals educated the committee on the fact (which must not have come as a surprise to those committee members who have tax-deferred retirement accounts) that it is both a common practice, and generally viewed as a best practice, for individual investors to "buy and hold" securities and other investment assets. In addition, industry representatives informed the drafting committee that both the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority, Inc. (FINRA)[122] premise required outreach to "lost security holders" based upon a transfer agent's or broker-dealer's receipt of returned mail,[123] and that this standard is the federal regulators' proxy for a potential dormancy determination with respect to securities. This being the case, RUUPA premises the running of a dormancy period for securities upon the second instance of returned mail being received by the security holder.[124]

In instances where the owner of securities does not receive paper "snail mail," but has instead opted to receive communications electronically, RUUPA requires an alternative protocol designed to confirm that electronic communications are being successfully transmitted, no later than two years following the last recorded indication of an owner's interest in the property; in the event of a delivery failure or non-response, the fallback requirement

[122] FINRA describes itself as a not-for-profit organization created by Congress, "dedicated to investor protection and market integrity through effective and efficient regulation of broker-dealers." *About FINRA*, Fin. Industry Reg. Authority, last accessed June 3, 2018, https://www.finra.org/about.

[123] SEC Rule 17Ad-17 embodies the returned mail (RPO) standard and the attendant outreach requirements for a transfer agent of broker-dealer that receives returned mail. 17 C.F.R. § 240.17Ad-17 (2018); *cf.* Lost Securityholders and Unresponsive Payees, Exchange Act Release No. 34-68668, 2013 WL 176305 (Jan. 16, 2013) (describing the release of amendments to Rule 17Ad-17 in 2013 to expand its application and explains how the rule operates).

[124] Section 208(a) states:

> Subject to Section 210, a security is presumed abandoned three years after:
>
> (1) the date a second consecutive communication sent by the holder by first-class United States mail to the apparent owner is returned to the holder undelivered by the United States Postal Service; or
>
> (2) if the second communication is made later than 30 days after the first communication is returned, the date the first communication is returned undelivered to the holder by the United States Postal Service.

RUUPA § 208(a).

is to mail a communication using first class U.S. mail.[125] If this mailing is unsuccessful, the return-mail triggers running of the dormancy period for the owner's securities or brokerage account.[126] As the ULC drafting committee concluded, "The 1995 Act was not clear on when the running of the dormancy period for securities was triggered. Section 208 clarifies the trigger event and will help to reduce compliance challenges faced by holders."[127]

Given the more conservative "RPO" trigger that applies to this category of property, in contrast to RUUPA's generally applicable owner inactivity standard to assess dormancy, an ancillary question becomes what constitutes a "security."[128] It has been the case that some state administrators have refused

[125] Section 208(b) states:

> If the holder does not send communications to the apparent owner of a security by first-class United States mail, the holder shall attempt to confirm the apparent owner's interest in the security by sending the apparent owner an electronic-mail communication not later than two years after the apparent owner's last indication of interest in the security. However the holder promptly shall attempt to contact the apparent owner by first-class United States mail if:
>
> (1) the holder does not have information needed to send the apparent owner an electronic-mail communication or the holder believes that the apparent owner's electronic-mail address in the holder's records is not valid;
>
> (2) the holder receives notification that the electronic-mail communication was not received; or
>
> (3) the apparent owner does not respond to the electronic-mail communication not later 30 days after the communication was sent.

Id. § 208(b).

[126] Section 208(c) provides: "If first-class United States mail sent under subsection (b) is returned to the holder undelivered by the United States Postal Service, the security is presumed abandoned three years after the date the mail is returned." *Id.* § 208(c).

[127] *Id.* § 208 cmt.

[128] At base, section 102(27) defines "security" to include:

> (A) a security as defined in [insert citation to appropriate section of Article 8 of the Uniform Commercial Code];
>
> (B) a security entitlement as defined in [insert citation to appropriate section of Article 8 of the Uniform Commercial Code], including a customer security account held by a registered broker-dealer, to the extent the financial assets held in the security account are not:
>
> > (i) registered on the books of the issuer in the name of the person for which the broker-dealer holds the assets;
> >
> > (ii) payable to the order of the person; or
> >
> > (iii) specifically indorsed to the person; or
>
> (C) an equity interest in a business association not included in subparagraph (A) or (B).

Id. § 102(27). The Reporter's Comment to this section explains that the definition "intends to capture certain existing definitions found in the Uniform Commercial Code as well as equity interests in business associations not otherwise covered." *Id.* § 102 cmt.

to apply an RPO trigger to securities held within a brokerage account, and have only applied their statutory RPO trigger to securities issued by a company that are record-kept by transfer agents, pursuant to a strict reading of their statutes. While this differential application might strike the reader as discriminatory or unprincipled in effect, the problem has been resolved through RUUPA's clarification that the term "security" broadly includes individual securities that may be administered by a transfer agent as well as securities held in accounts that are held by registered broker–dealers.[129]

B. *Restrictions on Liquidation of Securities and Accounts*

The drafters of RUUPA took care to increase the level of post-escheat protections to owners of investment assets including securities through the design of a new and much more restrictive securities liquidation regime. The predecessor 1995 UUPA provided that an administrator may liquidate securities at any time prior to three years after the receipt of same, but if the administrator chooses to do so, a missing owner who subsequently claims the property "is entitled to the proceeds of the sale of the securities or the market value of the securities at the time the claim is made, whichever is greater."[130] As the comment to the 1995 UUPA explained, "Thus, there is a genuine incentive for an administrator to hold this property for the requisite three-year period."[131] Nevertheless, in practice there has been a tendency for states to liquidate securities much more quickly than three years post-escheat. In the most extreme instance on record, the State of Delaware was alleged to have liquidated securities escheated to it a mere three days after receipt of same—there, the State only refunded the liquidation value of such shares to the owners in response to their claims.[132]

RUUPA strictly requires that an administrator not liquidate escheated securities "until three years after the administrator receives the security and gives the apparent owner notice under section 503 that the administrator holds the security."[133] This change in policy was informed by evidence that owners of liquidated securities have asserted claims for the differential between the liquidation value of securities and their full market value (in instances where the market value has increased) from either or both the custodial state or the securities issuer or transfer agent that remitted the securities to the state.[134] Furthermore, advocates for owners and holders of securities argued that the

[129] It is important to note that mutual fund shares are also included in the definition of securities and hence an account that is held by a mutual fund company's third party administrator also gets this same beneficial dormancy trigger.

[130] UUPA § 12(b).

[131] *Id.* § 12 cmt.

[132] Complaint at 29, JLI Invest, S.A. v. Cook, No. 11274 (Del. Ch. July 9, 2015), https://finance.delaware.gov/publications/opinions/1652%20JLI%20&%20LIN.pdf

[133] RUUPA § 702(a).

[134] *See, e.g.*, JLI Invest S.A., v. Computershare Trust Co., No. 1:15-cv-11474, 2017 WL 354008 (D. Mass. Jan. 27, 2017).

state's liquidation of an escheated security exceeds the state's custodial authority, effectively removes the owner from his or her elected market position, and may effectuate a loss in value of the property (property that may have been purchased with a "buy and hold" philosophy) that is being relied upon as a form of retirement savings.

While RUUPA represents an improvement that inures to the benefit of owners of securities, the question remains: Why would a state would ever liquidate these property interests at all? Or, in the alternative, why the administrator is not being required to make the owner whole, in instances where the post-liquidation value of escheated securities has increased as of the time the owner's claim to the property is made?

In addition, some of the states that have subsequently adopted or introduced RUUPA legislation in part have, unfortunately, tended to reject this clear process improvement and owner protection, reverting instead to liquidation provisions that permit or even require liquidation within very short timeframes (*e.g.*, 90 days post-escheatment, or "as soon as practicable" post-escheatment).[135] These issues will continue to attract attention and appropriate debate in state legislatures where RUUPA is introduced.

IX. Foreign Owned Property

RUUPA retains the authority of a state to take custody of and escheat foreign-owned property. This authority is inconsistent with the underlying principle behind RUUPA—to reunite missing owners with their property.[136] Moreover, allowing a state to take custody of and escheat foreign-owned property is problematic because it conflicts with established Supreme Court rules and runs afoul of constitutional provisions.

The relevant provision of RUUPA relating to the custodial taking and escheat of foreign-owned property is section 304, which reads:

> (a) . . . the administrator may take custody of property presumed abandoned, whether located in this state, another state, *or a foreign country*, if the holder is domiciled in this state or is this state or a governmental subdivision, agency, or instrumentality of this state, and
>
> > (1) another state or foreign country is not entitled to the property because there is no last-known address of the apparent owner or other person entitled to the property in the records of the holder; or

[135] *See* 765 Ill. Comp. Stat. 1026/15-702(a) (2018) (permitting the administrator to liquidate a security prior to the expiration of the three-year period if the administrator determines it would be in the "best interests of the owner"); D.C. Council B. B22-0654, 22d Council Period § 702 (D.C. 2018) (establishing a 60-day holding period before liquidation of securities); H.B. 2486, 65th Leg. § 702 (Wash. 2018) (requiring the administrator to liquidate securities as soon as practicable).

[136] *See* RUUPA prefatory cmt. pp. 1-2.

> (2) the state or foreign country of the last-known address of the apparent owner or other person entitled to the property does not provide for custodial taking of the property.
>
> (b) Property is not subject to custody of the administrator under subsection (a) if the property is specifically exempt from custodial taking under the law of this state or the state or foreign country of the last-known address of the apparent owner.[137]

The drafters of RUUPA did, however, attempt to mitigate some impact of including foreign-owned property in escheatable property to a state of domicile.[138] Specifically, section 304 includes a new limitation that a state of domicile cannot escheat property in a foreign country if the foreign country "does not provide for custodial taking of the property" or the property is "specifically exempt from custodial taking under the law of . . . [the] foreign country of the last-known address of the apparent owner."[139] Nevertheless, section 304 fails to define what constitutes providing for "the custodial taking of property" or when property is "specifically exempt" from custodial taking in a foreign nation. At its core, RUUPA fails to acknowledge the exclusive right of a foreign nation to take custody of and escheat unclaimed or abandoned property of an owner in that country.[140] RUUPA, instead, endorses the imposition of a U.S. state's law on foreign-owned property unless that foreign nation has specifically addressed the ability to take custodial possession of unclaimed property. For the following reasons, this limitation does little to address the concerns of holders, including certain jurisprudential and constitutional issues.[141]

First, the Supreme Court set forth the exclusive priority rule in *Texas v. New Jersey*.[142] Under that rule, unclaimed property escheats first to the state of the last-known address of the apparent owner, as shown in the holder's

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[137] *See id.* § 304 (emphasis added); *see also id.* § 302 (permitting a state to escheat property located in a foreign country if the last-known address of the apparent owner is in that state).

[138] *See id.* § 304 cmt. (stating, in the official drafters' commentary to section 304, "Section 304(3)(b) adds a new provision that, if property is specifically exempt under the laws of either a state or foreign country in which the last known address of the owner is located, the state of holder's domicile cannot take custody. *See* N.J. Retail Merchs. Assn. v. Sidamon-Eristof, 669 F.3d 374 (3d Cir. 2012).").

[139] *See id.* § 304(a)(2), (b).

[140] It bears noting that encroachment on a foreign nation's rights raises due process concerns because United States courts cannot protect a foreign holder or owner in a foreign jurisdiction. *See* U.S. Const. amend. XIV. Holders and owners can be subject to multiple, conflicting rules regarding the custodial taking and escheat of foreign-owned property. These concerns are particularly pronounced given the fact that escheatment is by nature a deprivation of property.

[141] It should be noted that the state of domicile's ability to escheat foreign property is limited under RUUPA, like the 1995 Act, because the act does not apply to property in a foreign country arising out of a "foreign transaction." *See* RUUPA § 103 ("This [Act] does not apply to property held, due, and owing in a foreign country if the transaction out of which the property arose was a foreign transaction.").

[142] 379 U.S. 674 (1965); *see* Part VI *supra*.

books and records, and second, to the holder's state of domicile where either (1) the last known address of the owner of the property is unknown or (2) the owner's "last known address is in a state which does not provide for escheat of property."[143] Under a plain reading of this rule, escheatment of foreign-owned property is not permitted. By contrast, the official comment to section 304 states that the escheatment of foreign-owned property under section 304 is a "natural extension" of the *Texas v. New Jersey* priority rule.[144] This statement, however, is entirely unsubstantiated and unsupported by case law. The Supreme Court has never suggested that the state of domicile has the right to escheat property if the owner's address is in a foreign country. Rather, the Supreme Court has repeatedly declined to extend the priority rule it established in *Texas v. New Jersey*.[145] RUUPA's inclusion of foreign-owned property as escheatable to a state of domicile is simply contrary to the well-settled exclusive priority rule.

Second, the drafters of RUUPA address, but then dismiss in a straw-man like fashion, the decision of the Supreme Court in *Zschernig v. Miller*,[146] concerning a state's ability to tie its law to the law of a foreign nation and which implicates foreign relations. At issue in *Zschernig* was an Oregon statute that required the state to determine whether a foreign nation would grant reciprocal rights to a U.S. citizen upon testamentary disposition of property of a decedent.[147] The Court struck down the Oregon law because it had "more than 'some incidental or indirect effect on foreign countries' and [has] great potential for disruption or embarrassment" to the nation's foreign affairs.[148] Despite the drafters' assertion that "the rationale used by Court in [*Zschernig*] is neither controlling nor compelling in the context of unclaimed property,"[149] the decision is pertinent to the constitutionality of section 304. Here, RUUPA requires a state to evaluate both whether a foreign country has unclaimed property laws and whether such laws "specifically exempt" the property from escheat. Indeed, this is precisely the type of reliance on foreign law to determine state law consequences that the Supreme Court rebuked in *Zschernig*. Furthermore, there can be no doubt that a custodial taking or escheat of foreign-owned property implicates foreign affairs and risks non-uniform laws and retaliatory action by foreign nations.

Third, a state's ability to take custody of or escheat foreign-owned property raises significant Foreign Commerce Clause concerns. The Commerce Clause of the United States Constitution provides that Congress shall have

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[143] 379 U.S. at 680-82 (emphasis added).

[144] *See* RUUPA § 304 cmt.

[145] *See* Delaware v. New York, 507 U.S. 490 (1993); Pennsylvania v. New York, 407 U.S. 206 (1972).

[146] 389 U.S. 429 (1968).

[147] *Id.* at 430-31.

[148] *Id.* at 434-35.

[149] RUUPA § 304 cmt.

the power to regulate commerce "with foreign Nations."[150] The Supreme Court considered a state's regulation of foreign property with respect to a fairly-apportioned ad valorem property tax in *Japan Line, Ltd. v. County of Los Angeles*.[151] In *Japan Line*, California sought to impose a fairly-apportioned ad valorem property tax on containers owned by Japanese shipping companies that were temporarily present in California during their movement in foreign commerce.[152] The Court struck down the tax, cautioning states against imposing taxes where there is an "enhanced risk" of multiple taxation and where it may impair the Federal Government's ability to "speak with one voice" when regulating commercial relations with foreign governments.[153] The Court recognized that additional considerations must factor into the Court's analysis when a state seeks to regulate property owned by foreign citizens. Such an analysis is equally applicable in the unclaimed property context as the taking of foreign-owned property would implicate federal relations with foreign governments.

In short, a foreign nation is the exclusive authority to claim abandoned property owed to its citizens, not a U.S. state. The inclusion of a state's ability to escheat foreign-owned property in RUUPA is plainly contrary to Supreme Court jurisprudence and raises significant constitutional concerns.

X. Use of Contingent-Fee Auditors

Unclaimed property laws should encourage voluntary compliance and seek to reunite property with its rightful owners. And the Task Force encourages states to, where appropriate, audit holders in a manner that furthers those two goals. The use, however, of contingent-fee auditors and egregious estimation and projection methodologies fails to further these goals and should be avoided. Since the earliest days of this country, the use of contingent-fee auditors has been recognized as bad public policy.[154] More recently, the use of contingent-fee auditors has been held to raise significant due process concerns, given the financial stake that the auditor has in the outcome of the audit.[155] And, along with the use of egregious estimation and projection methodologies and other factors, the use of contingent-fee auditors has been ruled to "shock the conscience"[156] and results in assessments of unclaimed property

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[150] U.S. Const. art. I, § 8, cl. 3.

[151] 441 U.S. 434 (1979). *Japan Line* and its restrictions on the regulation of foreign commerce has been limited in the case of sales and use and income taxes. *See* Itel Containers Int'l Corp. v. Huddleston, 507 U.S. 60 (1993); Container Corp. v. Franchise Tax Bd., 463 U.S. 159 (1983). *Japan Line* has never been overruled.

[152] *Id.* at 436-437.

[153] *Id.* at 446-49, 452.

[154] *See* Benjamin Franklin, Rules by Which a Great Empire May Be Reduced to a Small One (1773), *reprinted in* 6 The Works of Benjamin Franklin, Correspondence and Miscellaneous Writings 1772-1775, 204 (John Bigelow ed., G.P Putnam's Sons 1904).

[155] Plains All Am. Pipeline L.P. v. Cook, 866 F.3d 534 (3d Cir. 2017).

[156] Temple-Inland, Inc. v. Cook, 192 F. Supp. 3d 527 (D. Del. 2016).

that will never be returned to its rightful owner. RUUPA, in section 1009(e), specifically allows the use of contingent-fee auditors, and the Subcommittee would encourage the removal of that provision.

By its very nature, the use of contingent-fee audit arrangements creates a conflict of interest when the auditor conducting the review of compliance with the unclaimed property law has a direct pecuniary interest in the results.[157] This encourages auditors to aggressively overinflate the assessment, because the larger the assessment, the larger the fee the auditor will receive. Specifically, the auditor is rewarded by interpreting state laws to its own advantage rather than in the state's best interest; ignoring holder errors that would result in lower assessments; and using egregious estimation and projection methodologies. The risk of abuse creates a perception of unfairness that colors holders' relationships with administrators and creates an atmosphere of mistrust that hinders compliance.

An example of contingent-fee auditors overinflating an assessment using an egregious estimation and projection methodology can be found in *Temple-Inland, Inc. v. Cook*.[158] In that case, a contingent-fee auditor hired by Delaware audited the holder for a 22-year period from 1986–2007, but the holder was only able to produce complete records back to 2003 for accounts payable and 2004 for payroll. On audit of the period for which the holder had records, the auditor found that an additional $147.30 was owed to Delaware. After the auditor finished extrapolating that one $147.30 mistake to the period for which the holder did not have records, the holder was initially assessed $2,128,834.13. The auditor's estimation methodology relied heavily on property escheatable only to other states to increase the amount of unclaimed property owed to Delaware.[159] In other words, the methodology used assumed 1) that all unclaimed property projected to the reach-back years should have been reported to Delaware and 2) that the holder did not file any unclaimed property reports. The court noted, "An estimation is properly performed when it is based on the principle that the unclaimed property in the reach-back years has 'all the same qualities and characteristics' as unclaimed property in the base-years."[160] The court noted further that the auditors failed to apply this essential principle and stretched the definition of address unknown property to troubling lengths.[161] In its holding, the court held that Delaware and its auditors "engaged in a game of 'gotcha' that shocks the conscience."[162]

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[157] *See* Tumey v. Ohio, 273 U.S. 510, 515, 523 (1927) (holding that the due process clause is implicated when a person fining another has a direct interest in the fine imposed).

[158] 192 F. Supp. 3d 527 (D. Del. 2016).

[159] *Id.* at 537.

[160] *Id.* at 548-49 (citing United States v. Mehta, 594 F.3d 277, 283 (4th Cir. 2010); *In re* Chevron U.S.A., Inc., 109 F.3d 1016, 1019-20 (5th Cir. 1997)).

[161] *Id.* at 549.

[162] *Id.* at 550.

The Subcommittee is not suggesting that all estimation should be barred in all cases. Rather, states should avoid egregious methods of estimation where, as in the *Temple-Inland* case, characteristics that favor liability are replicated across the whole, but characteristics that reduce liability are ignored. In addition, as the Court in *Temple-Inland* noted, the "use of estimation will not make it easier for owners to be reunited with their abandoned property, and may, in fact, make it harder."[163] If unclaimed property remitted to the state is not associated with a name or an itemized list identifying individual property, but is only part of an estimated bulk amount, it would be nearly impossible for an individual owner to recover unclaimed property from the state. Indeed, in *Temple-Inland*, the state was unable to give a single example of when estimated property was returned to an owner.[164]

Not only is the use of contingent-fee auditors bad public policy, it may also constitute an unconstitutional due process violation. In the recent case of *Plains All American Pipeline L.P. v. Cook*, the U.S. Court of Appeals for the Third Circuit held that a procedural due process challenge to the appointment of a contingent-fee auditor to conduct an unclaimed property audit is ripe for review, and the United States District Court for the District of Delaware erred in dismissing it.[165] The Court remanded the case to the District Court for further consideration.

Some states have expressed concern that they will not be able to conduct audits if they are not allowed to use contingent-fee auditors. They assert that it is not cost-effective to hire auditors paid on any basis other than on a contingent fee. This concern, however, is simply untenable. If it is cost effective for contingent-fee firms to not only hire and pay employees to conduct audits but to also earn a profit, it is certainly cost-effective for the state to hire individual auditors and pay them on an hourly basis or with a salary. And it would be more transparent to do so. States would be able to discern how much unclaimed property was assessed and how much it cost to hire the auditors as opposed to having auditor costs represented by a reduction in revenue.

XI. Unclaimed Property Laws Should Differ for Consumers and Businesses

The purpose of unclaimed property laws should be to return property to its rightful owners, thereby protecting consumers. Thus, it is appropriate for unclaimed property arising from transactions between a business and a consumer to be controlled by the states' unclaimed property laws. Transactions between two businesses, however, do not need to be controlled by a state's unclaimed property laws. This is similar to the states' consumer protection laws, which do not normally apply to business-to-business transactions

[163] *Id.* at 547-48.
[164] *Id.* at 548.
[165] Plains All Am. Pipeline L.P. v. Cook, 866 F.3d 534 (3d Cir. 2017).

because businesses do not need the same protections as consumers.[166] Instead, business-to-business transactions are already subject to another set of uniform laws, the states' Uniform Commercial Code (UCC). The UCC has rules that can differ from the states' unclaimed property laws. In contrast to businesses, consumers often do not have ongoing connections with a business holding their property or they lack an understanding of how to recover that property on their own, or both. Transactions between two businesses, however, are best settled by those two businesses, especially if those two businesses have an ongoing business relationship. When those two companies reconcile and settle their accounts, there is no need for a state to reopen those closed books and records years later to determine whether a business holds property that belongs to another business. Thus, property subject to the states' unclaimed property laws should differ based on whether the owner is a consumer versus a business enterprise.

There are several reasons why the states' unclaimed property laws should treat property owned by consumers differently from that owned by businesses. Transactions between a business and an individual consumer are typically not recorded on the books and records of the consumer. Transactions between businesses, however, are typically recorded on the books and records of those businesses in commercial accounts. Credit balances are common in commercial balance sheet accounts, which are represented as of a particular point in time (usually at the end of a fiscal period); however, they do not necessarily represent property due from one business to another. Instead, those credits usually represent a situation that will be resolved by the parties in their normal course of business—without the application of any legal remedy. For example, one business receiving a product from another business may show an extra item was shipped, which shows up on its accounting system as a credit due to the shipper. The shipper may have intentionally shipped the extra item in case another item is damaged during transit. The shipper may have accidentally shipped the extra item, but the situation is resolved on the next order. Or, the two businesses may resolve the discrepancy during the next fiscal period.

Some states aggressively assess such credit balances as unclaimed property, usually years later when the explanation for those credit balances has been lost to time. Sometimes the auditors make the issue worse by extrapolating the credit balances to periods for which the holder has no records. This aggressive audit activity generally turns into a windfall for a state as such amounts, even if they represent legitimate unclaimed property, are never able to be recovered by the owner. Because of this aggressive audit activity, eliminating

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[166] States' consumer protection laws apply to "consumers." *See generally* Carolyn L. Carter, Nat'l Consumer Law Ctr., Consumer Protection in the States: A 50-State Report on Unfair and Deceptive Acts and Practices Statutes (2009), http://www.nclc.org/images/pdf/udap/report_50_states.pdf.

the applicability of unclaimed property laws to business-to-business transactions is the single most important issue to the unclaimed property holder community.[167]

To the extent that the credit balances legitimately represent property due to another business and the parties do not resolve their disputes informally, remedies provided in other areas of the states' law already apply. All businesses are subject to the Uniform Commercial Code (UCC), which has been adopted in its entirety in 49 states and the District of Columbia. Additionally, Louisiana, with its unique civil code, has adopted most of the provisions but has maintained some of its own provisions governing the sale of goods.[168] The UCC provisions should control any unclaimed property aspects of business-to-business transactions. In most instances, UCC Article 2, which covers the sales of goods, business property owners' right to assert a claim to the other business generally expires four years after the cause of action has accrued.[169] In addition, businesses often have contractual provisions for how they will handle mismatched shipments and billings. These contractual agreements—not a state's unclaimed property laws—should control.

Unlike consumers, most businesses have the financial incentive and ability to collect what is owed from them when dealing with other businesses. Businesses constantly reconcile differences and have accountants and bookkeepers that monitor their transactions. These types of errors should not turn into a windfall to a state—which can easily occur when transactions are not matched to the business owner of the property or statistical extrapolation is used that makes it impossible for any potential owner to claim its ownership to such property, or both. Consequently, the burden for policing business-to-business transactions, unlike business-to-consumer transactions, should rest with the business community. Unlike some consumers, businesses have the incentive to monitor their financial affairs.

A state's decision to apply its unclaimed property law to transactions between businesses also impacts the costs of doing business in that state. States like North Carolina and Ohio have reduced the costs of doing businesses in the state by adopting a business-to-business exemption. In contrast, over 35 states have no or very limited business-to-business exemptions. Those states lacking a good business-to-business transaction exemption ultimately

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[167] *See* Douglas L. Lindholm & Ferdinand S. Hogroian, Council on State Taxation, The Best and Worst of State Unclaimed Property Laws: Cost Scorecard on State Unclaimed Property Statutes (2013), http://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/cost-scorecard--the-best-and-worst-of-state-unclaimed-property-laws-october-2013.pdf.

[168] *See* Samuel D. Brickley & Brian M. Gottesman, Business Law Basics, loc. 19: Uniform Commercial Code (2017) (ebook), http://www.businesslawbasics.com/chapter-19-uniform-commercial-code. Article 2 of the UCC places a greater burden on businesses that deal regularly with the types of goods being sold because such businesses are presumed to be more sophisticated and have the advantage of more contractual information.

[169] U.C.C. § 2-725 (Am. Law Inst. & Unif. Law Comm'n 1977).

increase consumer costs because the business community conducting its operations in those states ends up passing those costs on to its customers.

XII. Conclusion

The Task Force has been monitoring RUUPA and concludes that some of the RUUPA provisions would advance the administration of unclaimed property laws in the states. Nevertheless the states should not adopt RUUPA, at least not without modification, because of significant concerns about some of RUUPA's provisions.

As discussed in this Article, state administration of unclaimed property laws has become controversial in recent times. While RUUPA represents, in many respects, an improvement over prior law, RUUPA does not represent a consensus among interested parties. Indeed, significant concerns about some of RUUPA's provisions remain.

The unclaimed property law area is expanding in its reach, and controversies seem to be increasing as well. Thus, as states seek to enact RUUPA, lawmakers should carefully consider the concerns discussed in this Article and alter the legislation to reflect needed changes to the provisions found in RUUPA.