

## Unclaimed Property

### What Every Company Should Know About the Risks of a Multistate Audit

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All 50 states require companies to comply with broad and often complex unclaimed property (escheat) laws that mandate annual reporting. As we noted in our mailing of April 23, 2010 (click [here](#) to view), states can seek payments from companies that may reach tens of millions of dollars. But while states are becoming increasingly vigilant with respect to ensuring compliance, case law dealing with unclaimed property compliance remains sparse. The recent decision of Delaware Chancellor Leo E. Strine on February 2, 2012, in *Staples, Inc. v. Cook, et al.*, accordingly merits review. Below we provide a brief overview of a few of the basic escheat principles and then discuss the case.

#### Unclaimed Property Defined

Unclaimed property generally is defined as tangible or intangible property that has gone unclaimed by its rightful owner for a specified period of time. States typically focus on recovering intangible property, which includes (i) general ledger property and (ii) unclaimed equity. Every state has its own statutory definitions of what constitutes unclaimed, or escheatable, property. The most common general ledger abandoned property collected are unused customer credits or refunds (accounts receivable), uncashed vendor checks (accounts payable) and uncashed wage checks (payroll). On the equity side, abandoned property includes, among other things, uncashed dividends, dormant shareholder accounts, unclaimed merger consideration and unredeemed bonds. In addition, states focus on different types of unclaimed property that are industry specific. For example, among other things that states may target are unclaimed insurance proceeds (including annuities, life policies and death claims) and unredeemed gift certificates or rebates.

#### Reporting Rules

The United States Supreme Court created a two-tier priority scheme for reporting intangible unclaimed property. See *Texas v. New Jersey*, 379 U.S. 674 (1965); *Delaware v. New York*, 507 U.S. 490 (U.S. 1993). Under the primary rule, unclaimed property is reported to the state of the owner's last known address as shown by the debtor's books and records. However, if the owner's address is unknown or if there is an incomplete address, the unclaimed property is reported to the company's state of incorporation. Pursuant to these rules, unclaimed property is of particular interest in the states where either (i) a company is incorporated or (ii) a large percentage of its customers or shareholders are located based on the company's records.

#### Delaware Court of Chancery Weighs In On Rebates

On February 2, 2012, the Delaware Court of Chancery issued a decision, *Staples, Inc. v. Cook, et al.*, which resolved the question of whether certain "rebates" issued by Staples, Inc. to business customers were escheatable to the state of Delaware. Specifically, in October 2005, the state of Delaware commenced an audit for unclaimed property held by

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Staples, and by 2010, the State completed its audit on certain property types and sent Staples a demand for payment. Instead of paying the State, Staples brought a lawsuit against the State arguing that certain rebates were not unclaimed property under Delaware’s escheat statute (Escheat Statute) and therefore it was not obligated to pay the State for this liability. Central to Staples’ argument was its contention that the statute of limitations as to the rebates had run against the rightful owners and that the Escheat Statute did not allow Delaware to escheat property as to which a claim by the rightful owner would be time barred. Delaware disagreed and countersued, seeking a declaration that its demand was proper.

Chancellor Strine answered the “core” question of whether a statute of limitations argument would be relevant to the escheatment of the unclaimed rebates. He ruled in the State’s favor, finding that in these circumstances the statute of limitations was not relevant and that Staples had to escheat the property to the State. Specifically, Chancellor Strine explained that the “running of the statute of limitations against the owner [is] irrelevant when the property at issue is one of the specifically enumerated types” set forth in the Escheat Statute (in particular, § 1198(11)). Because Chancellor Strine found the unclaimed rebates to be, in Staples’ circumstances, either “bills of exchange” (*i.e.*, checks) or “credits,” both of which fall within the enumerated categories of what is escheatable property under the Escheat Statute, they were subject to escheat. Chancellor Strine further explained that the “reason why the property was given is irrelevant” to the analysis, and that what matters is whether the property falls within one of the enumerated unclaimed properties under the Escheat Statute – which, in this case, it did.

This decision further confirms that it is important for companies to fully understand escheat laws in order to grasp their potential exposure to unclaimed property liability, which can be asserted by a state long after traditional time bars for private claims have elapsed. It also demonstrates that courts will apply the letter of the law and order compliance if necessary.