McNees Wallace & Nurick LLC
75th anniversary

Harrisburg, PA • Lancaster, PA • State College, PA • Hazleton, PA • Columbus, OH • Washington, DC

APRIL 2010

PA TAX LAW NEWS

UNCLAIMED PROPERTY REPORTING - ARE YOU IN COMPLIANCE?
(PENNSYLVANIA REPORTS DUE APRIL 15)

By Sharon R. Paxton

Most states require the holder of "abandoned" or "unclaimed" property to report (and remit) such property after the expiration of a certain number of years (the "holding period"). These "escheat" laws generally apply to any property which does not legally belong to the holder, although some states exempt certain types of property, such as gift certificates and business-to-business transactions. Examples of reportable property include dormant bank accounts, stocks and bonds, insurance premium refunds, uncashed payroll checks, uncashed accounts payable checks, uncashed operating fund checks, credit balances, customer deposits, uncashed death benefit checks and unused gift certificates or gift cards.

Reporting obligations for abandoned and unclaimed property (with the exception of tangible personal property) are generally governed by the laws of the state of the legal owner's last known address rather than the laws of the state where the property or the business is located. If the owner's address is unknown, or if the owner's state of residence does not require reporting of the property, the unclaimed property is reported to the holder's state of incorporation. The length of the "holding period" varies from state to state and by type of property.

In most states, the filing deadline for annual unclaimed property reports is November 1. However, the deadline for filing an Abandoned and Unclaimed Property Report with the Pennsylvania Treasury Department ("Department") is April 15.

Holding Periods in Pennsylvania

For most types of property, the dormancy or "holding period" is five years for Pennsylvania reporting purposes. Notable exceptions include wages and other compensation for personal services (2 years), court-ordered utility refunds (2 years), property distributable in the course of dissolution of a business association, financial institution, insurer or utility (2 years), gift certificates with a specified redemption period (2 years), burial accounts (5 years after the death of the owner), money orders (7 years) and travelers checks (15 years).

The Pennsylvania Disposition of Abandoned and Unclaimed Property Act (the "Act") permits holders, with the consent of the State Treasurer, to report and deliver unclaimed property prior to expiration of the applicable holding period. Requests for early remittance should be submitted to the Department on an Early Remittance Request form. The Department will not accept early remittance of securities.

Gift Cards/Certificates

In 2006, the Act was amended to provide incentives for businesses to issue gift certificates and gift cards that do not contain an expiration

continued on the next page

date and are not subject to post-sale fees and charges. "Qualified gift cards" and "qualified gift certificates" are now exempted from reporting requirements. A "qualified" gift card or certificate cannot contain an expiration date or any type of post-sale charge or fee, including, but not limited to, a service charge, a dormancy fee, account maintenance fee, cash out fee, replacement card fee or activation or reactivation fee. While issuers of qualified gift cards and certificates no longer have an obligation to remit unredeemed amounts to the Commonwealth, they are obligated to redeem the gift cards and certificates indefinitely. The consideration paid for a gift certificate or gift card which does not meet the above requirements becomes reportable as unclaimed property two years after expiration of its stated redemption period or five years after the date of issuance if no redemption period is specified.

Reporting Procedures

For unclaimed property reportable to Pennsylvania, a Report of Abandoned and Unclaimed Property ("Report") and remittance of the reported property must be filed by April 15 of the year following expiration of the holding period. Holders that do not timely report or remit unclaimed property may potentially be subject to interest and penalties. If applicable, interest is imposed at an annual rate of 12% from the date the property should have been reported. An Extension Request form is available for holders to request an extension of the filing deadline for a period of up to 90 days. (Extensions will not be granted for two consecutive years.)

The Department requests that companies reporting both tangible and intangible property file separate reports. Except with respect to travelers checks and money orders, the name, if known, and last known address, if any, of each person appearing from the holder's records to be the owner of any property valued at $50 or more must be specified in the Report. A description of the property must be included, as well as the date when the property became payable or returnable (or the date on which the property was declared or found to be without a rightful or lawful owner) and the date of the last transaction with the owner with respect to the reported property.

Electronic reporting is requested for holders with ten or more unclaimed property items to be reported. The Department will accept holder reports via e-mail, electronic file transfer or CD-ROM. Businesses that have no reportable unclaimed property for the year are generally required to file negative reports with the Department. Negative reports may be filed electronically through the Department's website.

There is no "de minimis" threshold for reporting items of unclaimed property. However, items with a value of less than $50 may be reported in the aggregate. That is, it is not necessary to supply the name and address of the individual "owners" of property valued at $49.99 or less on the Report. For those items, it is sufficient to report, for each type of property included on the Report, the total number of owners and the total aggregate dollar amount of the property. Charitable organizations are obligated to report and remit unclaimed property to the Department, but they are exempt from the requirement to file negative reports.

Due Diligence

Holders who are transfer agents for securities are required by Securities and Exchange Commission regulations to exercise reasonable care to determine the correct addresses of lost security holders for certain accounts. Although other holders are not required by the Act to search for lost owners, the Department encourages all holders to make reasonable efforts to locate owners prior to expiration of the holding period. (Deductions from the value of an owner's unclaimed property for search expenses are not authorized.) While most holders are not required to conduct "due diligence," the Department does request that a due diligence verification form be submitted with the Report, listing any attempts to contact owners of the unclaimed property prior to filing the Report. In the case of reported property for which no attempt was made to contact the owner(s), the verification form requests a listing of the reasons for not conducting due diligence.

Audits/Estimation Procedures

In 2002, the Treasury Department was granted specific statutory authority to estimate a business' liability under the Act if the business fails to maintain the required records or if the available records are insufficient to permit the preparation of a report. In such cases, the Department may estimate the liability on the basis of available records or any other "reasonable" method of estimation. However, the Department bears the burden of proof regarding the estimation of the value of property subject to reporting requirements under the Act.

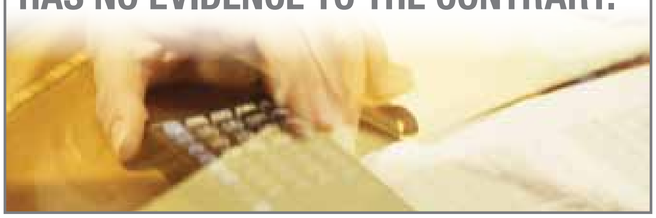
The Department has issued regulations pertaining to the estimation procedures to be used when an unclaimed property holder has insufficient records to determine its liability. However, the regulations merely provide that the sampling and estimation procedures used to determine a holder's liability "will be applied in accordance with standards of the American Institute of Certified Public Accountants (AICPA) and the United States General Accounting Office (USGAO)." 61 Pa. Code § 951.31(b). Those standards provide little in the way of detailed guidance for estimating liabilities in unclaimed property audits. The Department therefore believes it has wide latitude in determining estimation procedures.

The Department routinely posts copies of Audit Reports for unclaimed property audits on its website. Those reports list the name of the auditee, as well as the amounts for which it was found to be liable and its response to the audit results.

Claims by Property Owners

The Department is required to publish and mail notice to each Pennsylvania owner identified in a holder report who appears to be entitled to property with a value of $250 or more. In addition, all owners identified in holder reports are posted on the Department's website. Holders may make direct payments to the owners of unclaimed property that has been reported and remitted to the Department. Upon proof of payment and proof that the payee was entitled thereto, the Department will reimburse the holder for such payment together with interest (at the prevailing rate for tax overpayments) from the date of receipt of such proofs to a date within 30 days of the mailing date of the reimbursement.

... IN THE EVENT OF AN AUDIT, SUCH UNCASHED CHECKS WOULD BE PRESUMED TO BE REPORTABLE UNCLAIMED PROPERTY IF THE HOLDER HAS NO EVIDENCE TO THE CONTRARY.



First-Time Filers/Voluntary Disclosure

There is no "multi-state" voluntary disclosure program available for companies with unreported unclaimed property liabilities in multiple states. Many states have voluntary disclosure programs and/or a policy to waive interest and penalties for first time filers. However, each state has its own procedures and requirements, so a company with exposure in multiple states should investigate the particular requirements of each state in which it has a significant unreported unclaimed property liability.

In recent years, the Pennsylvania Treasury Department has conducted a substantial public education campaign and increased enforcement activity. For businesses that have never filed a Pennsylvania Report and would like to come into compliance, the Department offers a Voluntary Compliance Program ("VCP"). The standard agreement for the VCP provides that interest and penalties will be waived if the holder reports its unclaimed property in accordance with the terms of the agreement. To participate, a holder must complete a review of its books and records for at least ten years prior to the current report year, disclose all subsidiaries or entities included in the compliance review, disclose in writing all business positions, methodologies and estimation techniques (if applicable) and property types reviewed to determine the unclaimed property liability, and disclose any methods of due diligence performed. A report must be filed within 90 days after execution of the VCP agreement, and the participant must agree to be "fully compliant" with the Act going forward.

Planning for Unclaimed Property Reporting

Most businesses have at least a nominal unclaimed property liability for uncashed checks or credit balances. Companies that have not done so should establish internal accounting procedures to identify and track unclaimed property. Detailed recordkeeping with respect to the disposition of uncashed checks and other potential types of unclaimed property is critical, especially where records may not be available for earlier years that become the subject of an audit and where the liability for those years may be determined by "estimation." For example, some checks may have remained uncashed because they

continued on the back page

were issued in error, the underlying liability was voided or a replacement check was later issued. These items would not represent reportable "unclaimed property" if the surrounding circumstances were documented. However, in the event of an audit, such uncashed checks would be presumed to be reportable unclaimed property if the holder has no evidence to the contrary. For companies with incomplete records for prior years, an auditor's development of an "unclaimed property ratio" by, for example, comparing the amount of uncashed checks to a company's year-end accounts payable balance for years for which records are available and then projecting that ratio against year-end accounts payable balances for years for which records are not available, as a means of estimating the liability for such years, would exacerbate the impact of any such documentation deficiencies. The Department recommends the establishment of "liability accounts" to record and age uncashed checks until they become reportable to the Department as unclaimed property.

For advice concerning unclaimed property reporting obligations or assistance in dealing with an audit review or appealing an audit assessment, please contact Sharon Paxton (by email at spaxton@mwn.com or telephone at 717-237-5393) or another member of the McNees Wallace & Nurick State and Local Tax Practice Group. ■

Sharon R. Paxton is Vice-Chair of the State and Local Tax Group.
spaxton@mwn.com / 717.237.5393

SUBSCRIBE FOR EMAIL DELIVERY

To receive the *PA Tax Law News* Newsletter in your email please go to the "newsletter signup" page under the "newsroom" tab at www.mwn.com.

McNees State and Local Tax Group

James L. Fritz, Chair
717.237.5365 / jfritz@mwn.com

Sharon R. Paxton, Vice Chair
717.237.5393 / spaxton@mwn.com

Salvatore J. Bauccio
717.237.5238 / sbauccio@mwn.com

Timothy J. Horstmann
717.237.5462 / thorstmann@mwn.com

David R. Kraus
717.237.5290 / rkraus@mwn.com

Randy L. Varner
717.237.5464 / rvarner@mwn.com

Catherine E. Wright, Paralegal
717.237.5294 / cwright@mwn.com