

Morgan Lewis

Unclaimed Property
Reporting in Delaware

*Old Laws, New Property:
Escheat and Gift Cards*

presented by

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Overview

- Why Gift Cards?
- What State Law Applies?
- Structuring Gift Card Programs to Manage Compliance
- Problem Areas and Hot Topics

The Gift Card Phenomenon

- Wildly popular!
- Consumers like them:
 - Happy medium between cash and a particular gift
 - Gift cards are the most requested gift item of the past 5 years
- Retailers like them:
 - Extend holiday / giving seasons
 - Generate store traffic and drive revenue
 - “Uplift”
 - “Breakage”



How do escheat laws relate to gift cards?

- There are lots of unused gift cards
 - Generally 12-15% of gift card balances never redeemed
 - Reports indicate that the avg. household has \$300 worth of unused gift cards
 - Cash-strapped state governments have taken notice
- States have begun to claim the unused balance on gift cards (the “breakage”) as unclaimed property
- States differ in how they address gift cards:
 - Many treat it as unclaimed property, although in different ways
 - Some clearly exclude gift cards from unclaimed property laws
 - Delaware?
- *Does treating unused breakage as unclaimed property make sense?*

State Laws on Escheat of Gift Cards

- In light of the potential value of unredeemed gift cards, the question of which state's unclaimed property laws apply is critical
- Supreme Court has explained the rules for deciding which state gets escheat of unclaimed property:
 - First priority rule: State of the owner's last-known address
 - Second priority rule: If holder's records do not disclose, property is subject to the laws of the holder's domicile, e.g., state of incorporation

See Texas v. New Jersey, 379 U.S. 674 (1965).

Structuring Gift Card Programs to Manage Compliance

- Sell gift card liability to a third-party
- Or, establish a subsidiary that issues gift cards in a state that clearly has no escheat requirement, e.g., VA or FL
 - Consider type of entity (corporation, LLC etc.)
 - Maintain corporate formalities
 - Only operate in that state

Problem Areas and Hot Issues: New Jersey Legal Battles

- In 2010 New Jersey amended its escheat law regarding gift cards:
 - Gift cards presumed abandoned after 2 years
 - If holder's records did not disclose the owner's last-known address, escheat was to the place of purchase (rather than place of holder's domicile)
 - Data collection requirement
- Retail and industry groups sued to keep the law from taking effect
- Ultimately the Third Circuit Court of Appeals determined:
 - No retroactive application
 - No "place of purchase" rule
 - Data collection requirement Ok
- Showdown on the data collection requirement in 2012
- Compromise legislation, July 2012:
 - Data collection requirement postponed 4 years
 - Abandonment period increased from 2 to 5 years
 - Only 60% of the unredeemed balance on gift cards subject to escheat (rather than 100%)
 - Cash redemption on gift cards with less than \$5 in value

Problem Areas and Hot Issues: Online Sales and Registration of Gift Cards

- Changing retail environment may result in growing first priority liability:
 - The growth of internet purchases where “ship to” information is obtained
 - Also registration of gift card/loyalty, reward program
- Use of separate issuer entity?
- Use of customer limiting instructions regarding personal information?

Problem Areas and Hot Topics: Impact of Federal CARD Act

- The Credit Card Accountability and Responsibility & Disclosure Act of 2009 (“CARD Act”) and Regulation E imposed a number of restrictions on gift cards
 - One is that gift cards cannot expire less than 5 years after issuance or last load
- In August 2012, Bureau of Consumer Financial Protection issued intent to determine whether escheat provisions of ME and TN (are inconsistent with and preempted by the CARD Act):
 - ME: Gift cards are presumed abandoned two years after Dec. 31 of the year issued or the most recent transaction occurred. 33 M.R.S. § 1953.
 - TN: Gift cards are presumed abandoned if unclaimed as of the earlier of (a) the expiration date or (b) 2 years from issue. Tenn. Code Ann. § 6-29-135.
 - Problem: “[ME & TN] laws presume gift cards to be ‘abandoned’ and release businesses from the obligation to honor the gift cards during a time period when, pursuant to Federal law, consumer should be able to use the cards.” Notice of Intent, 12 CFR Part 1005



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