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UNCLAIMED PROPERTY: WHAT THE INSURANCE INDUSTRY NEEDS TO KNOW & BEST PRACTICES

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January 16, 2020

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Agenda

- Introduction
- Unclaimed Property Overview
- Unclaimed Property Regulators Target Insurance Industry
- Best Practices
- New Legislation

UNCLAIMED PROPERTY OVERVIEW

Unclaimed Property Introduction

General Information

- All 50 states, the District of Columbia, Puerto Rico, and the US Virgin Islands have enacted unclaimed property laws.
- The purpose of unclaimed property laws is to ensure the protection of abandoned property until the rightful owner is located. Moreover, states use any derivative funds earned on such property for the public good.
- States actively pursue unclaimed property as an additional source of revenue for the state, which avoids raising taxes.
- States' unclaimed property laws apply to all entity types, including:
 - Corporations
 - S Corporations
 - Partnerships
 - Limited Liability Companies

Unclaimed Property Introduction

What is Unclaimed Property?

- Intangible personal property for which there has been no owner activity for a specified period of time (“dormancy period”).
- General examples of unclaimed property:
 - Uncashed or voided payroll or commission checks
 - Uncashed or voided payable/vendor checks
 - Gift certificates/gift cards
 - Customer merchandise credits, layaways, deposits, refunds or rebates
 - Overpayments/unidentified remittances
 - Suspense accounts
- Examples of unclaimed property specific to insurance companies:
 - Unused/outstanding benefits (non-ERISA)
 - Insurance policies (e.g., life insurance, health insurance, property/casualty insurance)
 - Annuity payments
 - Matured endowments
 - Retirement accounts
 - Pension accounts

Unclaimed Property Introduction

Where Do I Report Unclaimed Property?

- The Supreme Court of the United States in *Texas v. New Jersey* established the following unclaimed property sourcing rule:
 - First, to the state of the rightful owner’s last known address, if known, or
 - Second, to the state of the holder’s incorporation (commercial domicile for unincorporated entities).
 - These priority rules were upheld in the subsequent cases *Pennsylvania v. New York* (escheat of money orders) and *Delaware v. New York* (unclaimed dividends and interest).
- Some state statutes include a transaction rule that gives priority to the state in which the transaction took place. However, the US Supreme Court in *Texas v. New Jersey*, *Pennsylvania v. New York*, and *Delaware v. New York* and the Third Circuit Court of Appeal in 2018 in *Marathon Petroleum v. Sec’y of State* held that only two states can escheat property: (1) the state of the owner’s address under the primary rule, and (2) the state where the holder is incorporated under the secondary rule. Note that Congress enacted federal legislation that modifies the priority rules for travelers checks, money orders, official checks, and similar instruments by adopting a transaction rule for those properties only.

Example of the Impact of Extrapolation - Gross

Year	Company Sales	Total Unremediated Unclaimed Property - All States	Unremediated Unclaimed Property w/ Delaware Address	Extrapolated Liability Sourced to Delaware	Total Delaware Assessment
2018	\$ 750,000,000.00	\$ 250,000.00	\$ 12,500.00	Use Actual Data	\$ 12,500.00
2017	\$ 700,000,000.00	\$ 650,000.00	\$ 5,500.00		\$ 5,500.00
2016	\$ 680,000,000.00	\$ 320,000.00	\$ 11,200.00		\$ 11,200.00
2015	\$ 675,000,000.00	\$ 90,000.00	\$ 8,300.00		\$ 8,300.00
2014	\$ 665,000,000.00	\$ 110,000.00	\$ 4,500.00		\$ 4,500.00
2013	\$ 550,000,000.00	Documents Unavailable	Documents Unavailable	\$ 225,072.00	\$ 225,072.00
2012	\$ 625,000,000.00			\$ 255,764.00	\$ 255,764.00
2011	\$ 600,000,000.00			\$ 245,533.00	\$ 245,533.00
2010	\$ 550,000,000.00			\$ 225,072.00	\$ 225,072.00
2009	\$ 540,000,000.00			\$ 220,980.00	\$ 220,980.00
2008	\$ 525,000,000.00			\$ 214,841.00	\$ 214,841.00
2007	\$ 510,000,000.00			\$ 208,703.00	\$ 208,703.00
2006	\$ 495,000,000.00			\$ 202,565.00	\$ 202,565.00
2005	\$ 475,000,000.00			\$ 194,380.00	\$ 194,380.00
2004	\$ 460,000,000.00			\$ 188,242.00	\$ 188,242.00
<u>Actuals</u>	\$ 8,800,000,000.00	\$ 1,420,000.00	\$ 42,000.00	\$ 2,181,152.00	\$ 2,223,152.00
<u>Error Rate</u>		0.04%			
<u>Application of Penalties and Interest</u>					1,116,576
<u>Total Delaware Assessment</u>					<u>3,339,728</u>

REGULATORS AND TARGET INSURANCE INDUSTRY

Regulators Target Insurance Industry

- New York State Department of Financial Services Investigation – 2011
- NAIC's Unclaimed Life Insurance Benefits Working Group
- Policy Locators
- Pension Close Out Transfers

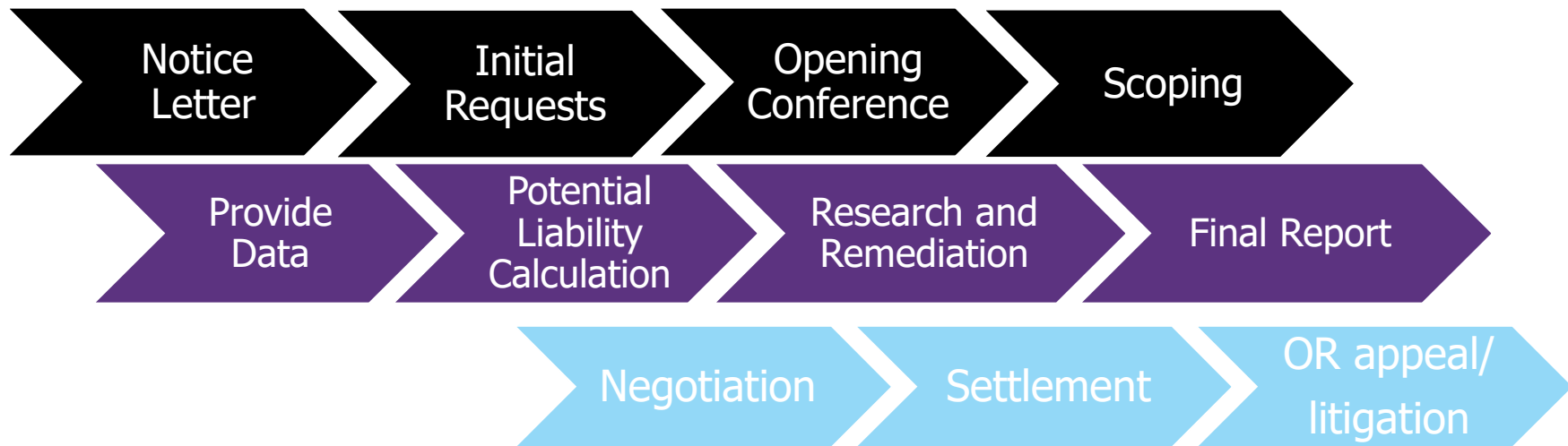
Unclaimed Property Audits

- States have broad authority to examine books and records for compliance
- States seek payment for unreported liability, including interest and potential penalties
- Increase in audits
 - State budget shortfalls causing states to reduce dormancy periods and add types of property subject to escheat
 - Estimates are that 80% of companies are not complying with unclaimed property laws
 - Use of sophisticated third-party audit firms representing multiple states on contingency fee basis
 - Use of “estimation” to determine multimillion-dollar liability where records are missing
 - Insurers in cross-hairs

Unclaimed Property Audits (cont.)

- An audit may be triggered by:
 - Publicity (M&A activity, lawsuit, new story, or investigation)
 - Lack of reporting history; errors or deficiencies in reporting
 - Industry targeting (e.g., life insurance, financial services, retail)
 - State of incorporation (particularly DE and NV)
 - Filing claims to recover unclaimed property

Unclaimed Property Audits (cont.)



An unclaimed property audit generally takes at least 2 years, often 3-5.

Unclaimed Property Litigation

- Major growth in litigation regarding unclaimed property issues.
- Companies fighting unfair audit tactics (e.g., *Temple-Inland*, *Marathon Petroleum*, *Office Depot*, etc.)
- False Claims Act litigation, pursued by state and/or whistleblowers

Voluntary Disclosure Agreements

- Offered and encouraged by most states, incl. DE and NY
- No interest and penalties
- Control over the review process
- Time

Problem Areas for Insurance Companies

- Life insurers: diligence on deceased policyholder for life insurers
 - Model Unclaimed Life Insurance Benefits Act, 2015
- Health insurers: credit balances for health insurers
 - Preemption and defenses
 - Drafting of payer agreements and overpayment letters
- Property & casualty insurers: settlement offers and owner ID

UNCLAIMED PROPERTY BEST PRACTICES

Unclaimed Property Best Practices

- The following best practices can be incorporated into all holder's compliance process to mitigate future escheat liabilities:
 - Understand Historical Unclaimed Property Compliance through Feasibility Review
 - What are the relevant property types at risk in the insurance industry?
 - Have we filed all property types for at least the last 10 years?
 - Identity, analyze, and remediate large balances
 - Establish Written Policies & Procedures
 - Accounting Practices & Control Reviews (Global Mapping)
 - Voluntary Disclosure Process

UPDATE - NEW LEGISLATION AND CASE LAW

Legislative Update

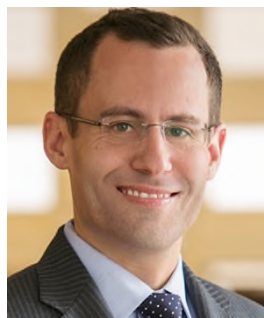
- Historically, dormancy periods ran from proof of death, knowledge of death, or a limiting age; affirmatively investigating the status of the insured was not required.
- In 2009, some states began requiring insurers to review the Social Security Administration's Death Master File (DMF) rather than wait for notice of death.
 - No statutory authority existed.
- National Counsel of Insurance Legislators (NCOIL) Model Unclaimed Life Insurance Benefits Act addresses the issue.
 - Many states require insurers to conduct semiannual DMF searches & fuzzy matching
- 2016 Revised Uniform Unclaimed Property Act (RUUPA) model act adopted.
 - Ties "knowledge of death" to a DMF review, for any purpose.
- Some states use the actual date of death to begin the dormancy period, rather than when the conditions obligating the insurer to pay are satisfied

Questions?



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Biography



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Ezra D. Church focuses his practice on class action lawsuits and complex commercial and product-related litigation, with particular emphasis on the unique issues facing retail, ecommerce, and other consumer-facing companies. Ezra also has experience handling all aspects of unclaimed property or abandoned property matters, including advice on developing legally-compliant systems to manage and minimize escheat obligations, representation of companies in state unclaimed property audits and voluntary disclosure agreements, and extensive experience litigating unclaimed property matters in courts throughout the United States.

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Scott Fischer works with members of the firm’s finance team focusing on multiple aspects of insurance representations, including restructuring and bankruptcy, transactional, and regulatory matters. Scott joined Morgan Lewis in 2018 following more than six years of service in state government, most recently serving as executive deputy superintendent for insurance at the New York State Department of Financial Services, where he led several hundred employees in supervising approximately 1,700 insurers operating in New York with assets exceeding \$4.2 trillion.

Prior to taking that post, Scott was first deputy general counsel and then special deputy superintendent at the New York Liquidation Bureau, where he managed a staff of more than 200 employees overseeing the liquidation proceedings of more than 25 domestic insurers, handling thousands of claims eligible for New York insurance security fund coverage, and distributing more than \$500 million in claim payments and estate dividends. Earlier government positions include senior counsel at New York State Insurance Department and assistant attorney general at the New York State Office of Attorney General. Scott began his legal practice as an associate at a number of other global law firms.

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Matthew S. Mock advises clients on state and local tax litigation and planning, regularly representing them in all stages of state and local tax controversies, including sales tax, income tax, and unclaimed property disputes. Matt is often called on to counsel on audits, protests before state administrative agencies, and appeals to state courts. He also advises multinational companies on the state and local tax aspects of corporate restructurings and transactions.

Matt provides guidance on the application of numerous state and local transfer taxes, in addition to issues created by the significant differences between state taxes and jurisdictional standards, as well as those presented by the United States and international tax regimes.

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Adam Beckerink represents clients, including multinational corporations and high net-worth individuals, in tax disputes, controversies, and litigation with revenue authorities throughout the United States. His practice spans all aspects of the tax planning and dispute resolution process, including audit, litigation, and appeals in matters including state False Claims Act tax defense, state tax refund class action defense, individual residency, telecommunications excise tax, and sales and income tax.

Through both litigation and settlement, he has resolved difficult state tax matters before administrative appeal boards, tax tribunals, and courts in Illinois and throughout the United States. Adam advises diverse US- and non-US-based multinationals on all aspects of state income, franchise, sales and use tax, and unclaimed property issues, including nexus, business/non-business income, unitary business principles, and US constitutional concepts. He also counsels on multistate and federal tax planning, and the tax aspects of mergers and acquisitions.

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Laura Grace Mezher advises multinational companies in a wide range of tax planning and controversy issues. In particular, Laura Grace focuses on issues concerning income tax, gross receipts tax, sales and use tax, franchise tax, excise tax, property tax, and unclaimed property matters. Before joining Morgan Lewis, she was an associate in the tax practice group of another global law firm.

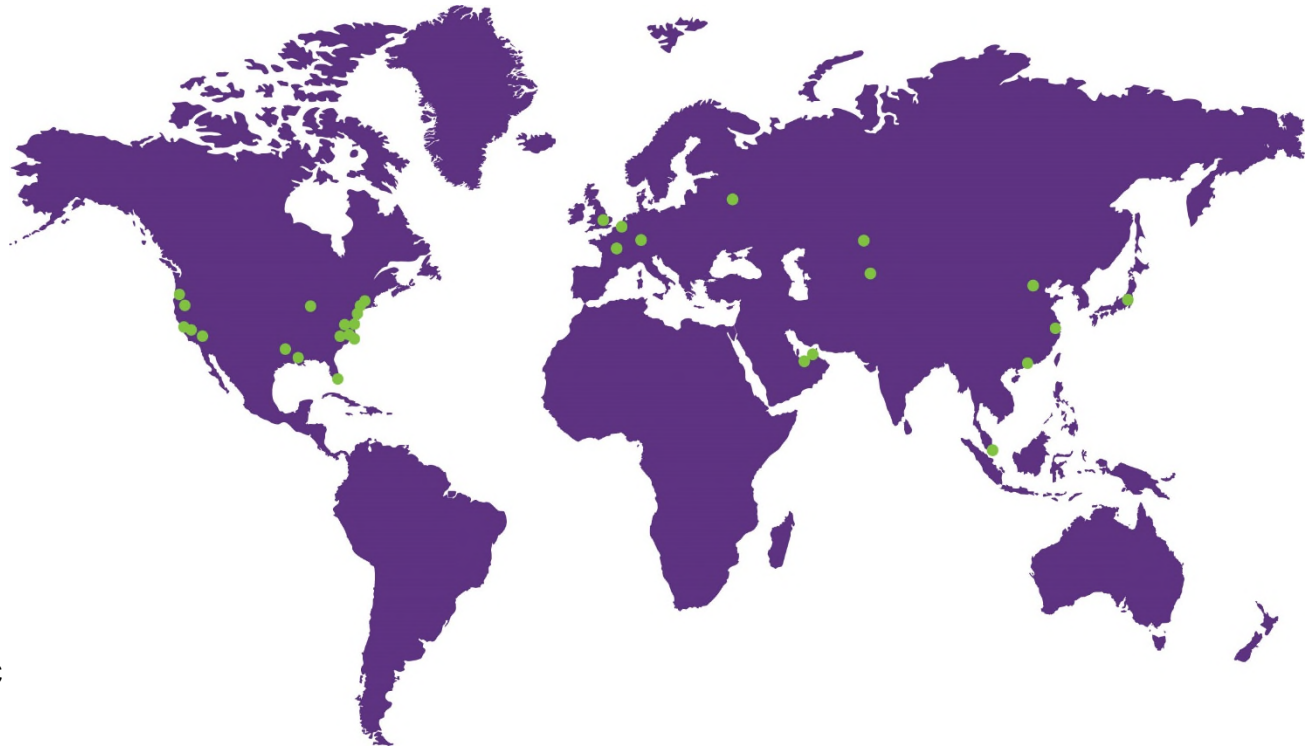
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