



## DELAWARE GENERAL ASSEMBLY

FINAL REPORT OF THE TASK FORCE TO STUDY  
AND MAKE FINDINGS AND RECOMMENDATIONS  
TO IMPROVE FAIRNESS AND COMPLIANCE IN  
DELAWARE'S UNCLAIMED PROPERTY PROGRAM

ESTABLISHED UNDER THE PROVISIONS OF  
SENATE CONCURRENT RESOLUTION No. 59,  
PASSED BY THE STATE SENATE AND  
THE HOUSE OF REPRESENTATIVES  
OF THE 147TH GENERAL ASSEMBLY,  
JUNE, 2014

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*Meeting of the Unclaimed Property Task Force in the Buck Library of the Buena Vista State Conference Center, New Castle, on October 2, 2014.*

# INTRODUCTION

The Unclaimed Property Task Force (the “Task Force”) was established by the 147th General Assembly via Senate Concurrent Resolution No. 59. In authorizing the Task Force, the General Assembly instructed it to inquire into, examine, study, and make findings and recommendations related to improving fairness and compliance in Delaware’s unclaimed property program.

This Report summarizes the work of the Task Force, which was comprised of members of the General Assembly, Cabinet-level members of the Governor’s administration, representatives on behalf of the Delaware public, and representatives of several private organizations. The members of the Task Force discharged their duties over the course of five meetings, and worked diligently, in good faith, and with the goal of identifying ways to improve fairness and compliance in Delaware’s unclaimed property program.

In the pages that follow, the findings and recommendations of the Task Force are set forth, as are summaries of each Task Force meeting. The summaries have been crafted to give readers an understanding of the depth and breadth of the issues examined by the Task Force. For those readers who are interested in more detail, the formal minutes of each meeting are also provided. We invite the reader to review the detailed minutes so as to understand more fully the hard work and thorough deliberation of the Task Force.

The Task Force Co-Chairs thank each and every member of the Task Force for service and participation in the course of the Task Force’s work. The Task Force identified several areas for improvement, as well as examples of recent improvement that may not have been widely known. It will be the responsibility of our elected and appointed officials to follow through on the thorough work of the Task Force and to examine and implement its recommendations. We accept that responsibility, and we look forward to fulfilling it in 2015.



Senator Bryan Townsend, Co-Chair



Representative Bryon Short, Co-Chair

December 23, 2014

FULL TEXT OF  
SENATE CONCURRENT  
RESOLUTION NO. 59



SPONSOR: Sen. Townsend & Rep. B. Short  
Sens. Blevins, Lavelle

DELAWARE STATE SENATE  
147th GENERAL ASSEMBLY

SENATE CONCURRENT RESOLUTION NO. 59

ESTABLISHING A LEGISLATIVE TASK FORCE TO STUDY AND MAKE FINDINGS AND  
RECOMMENDATIONS TO IMPROVE FAIRNESS AND COMPLIANCE IN DELAWARE'S UNCLAIMED  
PROPERTY PROGRAM.

1 WHEREAS, by virtue of the operation of federal common law, Delaware – as the State of incorporation for  
2 thousands of entities – has the right to collect unclaimed property (*e.g.*, uncashed checks, uncashed payroll checks,  
3 unapplied credits, and unused rebates); and

4 WHEREAS, the State has received an increasing amount of revenue from unclaimed property annually, through  
5 voluntary payment from companies as well as audits of companies, making unclaimed property the third largest revenue  
6 source for Delaware; and

7 WHEREAS, a significant number of companies domiciled in Delaware have not met their responsibilities under  
8 law to escheat unclaimed property to the State; and

9 WHEREAS, the General Assembly and Executive Branch departments are now engaged in efforts to bring more  
10 companies into compliance; and

11 WHEREAS, the State has an interest in identifying additional ways to improve compliance that will promote the  
12 stability and predictability of this revenue source; and

13 WHEREAS, the State recognizes that efforts to improve compliance, as well as the unclaimed property program  
14 more generally, should be fair, efficient and predictable for holders of unclaimed property.

15 NOW, THEREFORE:

16 BE IT RESOLVED by the Senate of the 147<sup>th</sup> General Assembly of the State of Delaware, the House of  
17 Representatives concurring therein, that an Unclaimed Property Task Force (“Task Force”) be established and empowered  
18 to inquire into, examine, study and make findings and recommendations to improve fairness and compliance in the State’s  
19 unclaimed property program.

20 BE IT FURTHER RESOLVED that the Task Force be composed of the following members:

21 1. A member of the Senate Majority (who shall serve as a co-chair) and a member of the Senate Minority (who  
22 shall serve as a member), as appointed by the President *pro tempore*;

- 23           2. A member of the House Majority (who shall serve as a co-chair) and a member of the House Minority (who  
24 shall serve as a member), as appointed by the Speaker of the House;
- 25           3. The Secretary of State or a designee appointed by the Secretary;
- 26           4. The Secretary of the Department of Finance or a designee appointed by the Secretary;
- 27           5. The Controller General or a designee appointed by the Controller General;
- 28           6. A representative from the Office of the Governor; and
- 29           7. Two members of the public, one as appointed by the President *pro tempore* and one as appointed by the  
30 Speaker of the House.

31           BE IT FURTHER RESOLVED that the President *pro tempore* of the Senate and the Speaker of the House jointly  
32 ask the leadership of each of the following organizations to designate a representative from each organization to serve on  
33 the Task Force:

- 34           1. The Delaware State Bar Association;
- 35           2. The Delaware State Chamber of Commerce;
- 36           3. The Delaware Bankers Association;
- 37           4. The Delaware Business Roundtable; and
- 38           5. The Uniform Law Commission.

39           BE IT FURTHER RESOLVED that the co-chairs of the Task Force, and those members designated by them, be  
40 responsible for guiding the administration of the Task Force by, at a minimum:

- 41           1. setting a date, time, and place for the initial organizational meeting;
- 42           2. supervising the preparation and distribution of meeting notices, agendas, requests for information, minutes,  
43 correspondence, and reports of the Task Force and scheduling and coordinating interviews with State employees and others  
44 knowledgeable about the matters within the scope of the Task Force; and
- 45           3. ensuring that a final report of the Task Force, containing any recommendations for legislative or executive  
46 action, is submitted to the President *pro tempore* of the Senate and the Speaker of the House of Representatives no later  
47 than November 1, 2014, with a copy to the Governor and to the Director of the Division of Research of Legislative Council  
48 and to the Delaware Public Archives.

49           BE IT FURTHER RESOLVED that the President *pro tempore* of the Senate and the Speaker of the House direct  
50 the necessary staff of both chambers to assist this Task Force.

#### SYNOPSIS

This resolution establishes the Unclaimed Property Task Force to inquire into, examine, study and make findings and recommendations related to improving fairness and compliance in Delaware's unclaimed property program.

Author: Senator Townsend

# Membership of the Unclaimed Property Task Force

## ***Description of Members' Affiliations:***

1 Senate Majority Member (co-chair)  
1 Senate Minority Member  
1 House Majority Member (co-chair)  
1 House Minority Member  
Secretary of State or a designee  
Secretary of Finance or a designee  
Controller General or a designee  
Representative of the Office of the Governor  
1 public member  
1 public member

## ***Appointing Authority:***

President Pro Tempore of the Senate  
President Pro Tempore of the Senate  
Speaker of the House of Representatives  
Speaker of the House of Representatives  
Secretary of State  
Secretary of Finance  
Controller General  
Governor  
President Pro Tempore of the Senate  
Speaker of the House of Representatives

The President Pro Tempore of the Senate and the Speaker of the House of Representatives jointly ask leadership of each of the following organizations to name a representative to serve:

Representative of the Delaware State Bar Association  
Representative of the Delaware State Chamber of Commerce  
Representative of the Delaware Bankers Association  
Representative of the Delaware Business Roundtable  
Representative of the Uniform Law Commission

## ***Appointed Members:***

Sen. Bryan Townsend (co-chair)  
Rep. Bryon Short (co-chair)  
Sen. Gregory Lavelle  
Rep. Jeffery Spigleman  
Secretary Jeff Bullock  
Secretary Tom Cook  
Mike Morton, Controller General  
Leonard Togman, Public Member  
Mr. Edward C. Ratledge, Public Member  
Stan Stevenson, Esq., DSBA  
Thomas Collins, DBA  
Michael Houghton, ULC  
Jordon Rosen, DSCC  
Robert Tuinstra, Jr., DBR  
Michael Barlow, Office of the Governor

## ***Representing/ Date of Appointment:***

Delaware State Senate, 07/15/2014  
Delaware House of Representatives, 07/16/2014  
Delaware State Senate, 07/15/2014  
Delaware House of Representatives, 07/17/2014  
Secretary of State, 07/11/2014  
Secretary of Finance, 07/14/2014  
Controller General, 07/12/2014  
President Pro Tempore, 07/18/2014  
Speaker of the House 08/01/2014  
Delaware State Bar Association, 07/14/2014  
Delaware Bankers Association, 07/08/2014  
Uniform Law Commission, 07/17/2014  
Delaware State Chamber of Commerce, 07/18,2014  
Delaware Business Roundtable, 07/22/2014  
Office of the Governor, 10/01/2014

## ***Unclaimed Property Task Force***

### ***Support Team:***

**Michelle Zdeb**, Legislative Assistant for the Delaware State Senate Majority Caucus, staffed the meetings, planned and coordinated the work of the Task Force, reviewed the Meeting Minutes and Report Materials and provided liaison services between the Task Force and public.

**Kathryn “Kiki” Evinger**, Legislative Aide for the Delaware House of Representatives Majority Caucus, summarized the Task Force meetings and assisted in staffing the meetings.

**Dick Carter**, Special Projects Director for the Delaware State Senate Majority Caucus, compiled and reviewed the Task Force Report.

**Alton Irvin**, Communication Assistant for the Delaware State Senate Majority Caucus, provided photography services during Task Force meetings.

# Unclaimed Property Task Force Findings

- Delaware derives a significant portion of its revenues from unclaimed property, which is Delaware's third-largest revenue source.
- Encouraging corporate compliance with unclaimed property laws and responsibilities is the stated paramount objective of the Delaware Department of Finance and the Delaware Department of State.
- Although changes have been made in recent years that have helped to address the concerns of Delaware-formed entities with various aspects of the unclaimed property auditing process, several concerns remain. These include, among others, the length of the "look-back" period in the auditing process, the dominance of one audit firm in Delaware's audit portfolio, and the lack of a manual that contains procedural guidelines for use by Delaware contract auditors and guidance to the holder community.
- Although changes have been made in recent years that have helped to facilitate the reunification of owners and their property, there remains room for improvement.
- In terms of expressing concerns about the auditing process, companies that are aware of their legal obligations yet still fail to file required annual unclaimed property reports are in a less sympathetic position than those companies who file reports annually and in good faith.
- For the auditing process, the Delaware Department of Finance recently has developed a focus on the largest Delaware-formed entities that regularly fail to file unclaimed property reports.
- The Delaware Department of Finance accepts full responsibility for the ultimate decisions made by the State and its contract auditors in the auditing process, and welcomes feedback (particularly detailed feedback) from Delaware-formed entities on the auditing process.
- Pursuant to current Delaware law, a company may appeal the findings of an audit (including request for payment) to an independent reviewer appointed by the Delaware Secretary of Finance. The Secretary may adopt or reject the reviewer's determination in whole or in part, a decision that the company can appeal to the Court of Chancery. The Court's review is limited to whether the Secretary's determination was supported by substantial evidence on the record.
- From 2008 to 2013, estimation of companies' liability for unclaimed property constituted, on average, approximately 15-20 percent of Delaware's total annual unclaimed property revenues, or approximately 80-85 percent of revenues from general ledger audits.
- One Task Force member—Edward Ratledge, professional econometrician and Director of the Center for Applied Demography & Survey Research (CADSR) at the University of Delaware—undertook a preliminary review and found nothing methodologically incorrect about the estimation methodology used by Delaware's largest contract auditor. Other Task Force members were not involved in that review and did not opine on the estimation methodology.
- As shared by the Council on State Taxation (COST), several Delaware-incorporated entities have expressed concerns about the same contract auditor's estimation methodology.
- Following active outreach by the Delaware Department of State to thousands of large Delaware-incorporated entities, more than 700 entities are now enrolled in the Department of State's Voluntary Disclosure Agreement (DOS VDA) program. More than one-third of letter recipients entered the DOS VDA program.

- The deadline for entry into the DOS VDA program has passed, and there is an open question whether another similar program should be developed.
- There may be opportunities to bring more of the auditing process in-house in order to achieve cost-savings for Delaware taxpayers. Similarly, the development of a program similar to the DOS VDA program or modifications to the Department of Finance’s VDA program present similar opportunities.
- There may be opportunities to increase competition in the contract auditor industry while still acknowledging the benefit to Delaware taxpayers from the skills and experience of the State’s current contract auditors.

## Unclaimed Property Task Force Recommendations

- By the end of calendar year 2015, the Delaware Department of Finance should complete the development of a detailed manual containing procedural guidelines for Delaware unclaimed property audits, and update its regulations accordingly, to ensure greater transparency and predictability as to what should be expected by holders during a Delaware unclaimed property audit. The Department should also ensure its contract auditors comply with this manual, and should publish this manual prominently on the Department of Finance’s webpages related to unclaimed property. In developing this manual, the Department should use a process that generates input from appropriate stakeholders and interested parties.
- The Delaware General Assembly should modify the appeals process outlined in the Delaware Code so as to provide a central role for third-party review, including replacing the Secretary of Finance as the final decision-maker in the administrative appeals process.
- The Delaware General Assembly should amend the Delaware Code to shorten the “look-back” period in Delaware unclaimed property audits, create a new VDA program in consultation with the Departments of Finance and State, and ensure the look-back periods in any ongoing VDA processes achieves an effective balance of incentives inherent in the two types of programs (audit and VDA).
- The Delaware General Assembly should examine the issue of instituting a “cooling off” period before State employees in senior positions with the State’s unclaimed property program are permitted to accept employment with any of the State’s contract auditors.
- The Delaware General Assembly should modify the statute of limitations so as to confirm that, for annually-filing holders, there must be indicia of fraud in the past six years of filed reports before there can be commencement of an investigation into records for earlier years.
- The Delaware Department of Finance should renegotiate downward the length of its current contracts with unclaimed property auditors so that no contract with said auditors is for a longer time period than five years per initial or renewed term. These same time periods should be included in new contracts entered into by the Department of Finance.
- The Delaware Department of Finance should achieve more balance among the contract auditors who provide services to its unclaimed property program. The Department should provide an annual update of this balance to members of the Delaware General Assembly.
- The Delaware Department of Finance should continue its efforts to enhance the reunification process for owners of unclaimed property, including the use of online options and more secure forms of reunification for

higher-value property. The Department should provide an update regarding these efforts to members of the Delaware General Assembly.

- The Delaware Department of Finance and Department of State should enhance their efforts to bring audit and VDA processes in-house, so as to ensure efficient expenditures of Delaware taxpayer funds and minimize expenditures on higher-cost contractors. Both departments should annually report the outcomes of their efforts to members of the Delaware General Assembly. The departments should also increase staffing levels, as needed, to achieve any of the other recommendations included in this Report.

## Summary of Meetings

**July 24, 2014** — The Task Force began its work with a discussion of the motivations behind its work: addressing concerns of individual Delawareans with the process of reclaiming their property and of Delaware corporations with the auditing process, balanced against unclaimed property being Delaware’s third-largest revenue source. Additional issues of concern are the terms of contracts between Delaware and its contract auditors (in particular, the length of the contracts) and the length and information scope of audits. Representatives from Governor Markell’s administration explained that there have been changes in recent years to encourage voluntary compliance rather than audits (such as the Voluntary Disclosure Agreement (VDA) option), but that audits are a necessary tool to encourage compliance by corporate entities. During open discussion, the Task Force discussed the nature of the companies currently targeted for audit (the very largest Delaware corporations) and the efforts being undertaken to encourage companies to enter the VDA program so as to achieve predictability of unclaimed property revenues. The Task Force also discussed: (1) the importance of hearing directly from Delaware corporations, and (2) the number and size of auditors under contract with the State, and the factors to bear in mind if the decision is made to diversity the State’s auditing work.

**August 12, 2014** — The Task Force received a presentation from Delaware’s Department of Finance. The DOF presentation provided a comprehensive review of issues relating to unclaimed property. The DOF explained that it would like to see more voluntary compliance and that a healthy enforcement program is necessary to increase that compliance. DOF is the ultimate decision maker during the auditing process (rather than the State’s contract auditors). All states use auditors, and nearly all utilize some element of contingent fees. The DOF provided details about how the scope of the auditing process works, including with regard to estimating earlier years’ liabilities. The Task Force next discussed the details of fee arrangements with Delaware’s contract auditors, as well as recent changes in DOF procedures to help reunite owners with their property. During open discussion, the Task Force discussed: (1) the balance between relying on contract auditors and bringing more of the auditing functions in-house for State employees to perform; (2) the challenges of building and maintaining in-house capabilities; (3) the possibility of shortening the look-back period for audits; (4) whether any such shortening would have an impact on corporations complying with their legal responsibilities to report unclaimed property; (5) the lack of much sympathy among Task Force members for corporations who are knowingly not complying with their legal responsibilities; (6) the merits behind a “best practices” manual for unclaimed property audits; and (7) the reasons corporations may be opting not to join the VDA program.

**September 10, 2014** — The Task Force received a presentation from the Council on State Taxation (COST). COST stated that it had engaged in efforts to convince representatives from individual member companies to attend the meeting, but that its efforts were unsuccessful. COST expressed concerns about the way audits involving contract auditors have unfolded, as well as with the statutorily-determined statute of limitations and the definitions of “unclaimed property.” COST also expressed specific concerns with the system of estimation employed in unclaimed property audits. The Task Force next received presentations from: (1) Verus Financial, a life-insurance unclaimed property auditing firm; (2) Kelmar Associates, an unclaimed property auditing firm;

and (3) the Unclaimed Property Professionals Organization (UPPO), a non-profit trade organization. During open discussion, the Task Force discussed: (1) the respective roles of the State, the auditor, and the company in the process of estimating unclaimed property; (2) the relative percentage of estimated unclaimed property in the total unclaimed property revenues received by the State; (3) the situation in which a company has disposed of records after a legally-authorized period of time and then is subject to an unclaimed property audit involving estimation; (4) the interrelationship between federal law (as determined by the U.S. Supreme Court) and state law in the area of unclaimed property; (5) the lack of concrete examples provided to the Task Force of aggressive auditing experienced by companies that had a history of filing unclaimed property reports; (6) the length of the contract between Kelmar and the State, and the potential impact this has on competition within the auditing industry and, thus, the cost to Delaware taxpayers of securing auditing services; and (7) details relating to the ways Kelmar conducts its estimation of unclaimed property liability.

**October 2, 2014** — The Task Force received a presentation from the Department of Finance, which included answers to questions raised in previous Task Force meetings (including those related to the relative percentage of estimated unclaimed property in the total unclaimed property revenues received by the State). Task Force member Ed Ratledge, Director of the Center for Applied Demography & Survey Research at the University of Delaware, reported that after a detailed examination of Kelmar’s estimation process he found nothing inappropriate with the methodology. Secretary of Finance Tom Cook reported a significant increase in recent years of the amount of property returned to holders by DOF. Additional discussion included the topics of: (1) details relating to the State selling shares of stock and returning the funds to the owner; (2) the need for owners to make an explicit claim for return of associated dividends; (3) a “best practices” manual for Delaware’s contract auditors; (4) a review of the profiles of Delaware’s various contract auditors; (5) the relative percentage of audits assigned to Delaware’s various contract auditors; (6) the merits of bringing more of the auditing functions in-house for State employees to perform; (7) the Department of State’s VDA program; (8) concerns relating to the current structure of the administrative appeals process; and (9) possible recommendations for the Task Force to include in its Final Report.

**December 2, 2014** — the Task Force engaged in open discussion and finalized its Report.

# Minutes of the Meeting of the Unclaimed Property Task Force of Thursday, July 24, 2014

Senate Hearing Room, Legislative Hall, 1:00 p.m. – 3:00 p.m.

## Meeting Attendance:

### Task Force Members present:

Senator Bryan Townsend  
Senator Greg Lavelle  
Secretary Jeffrey Bullock  
Controller General Michael Morton  
Jordon Rosen  
Michael Houghton, Esq.

Representative Bryon Short  
Representative Jeff Spiegelman  
Secretary Thomas Cook  
Stan Stevenson, Esq.  
Thomas Collins  
Leonard Togman, Esq.

### Absent:

Robert Tuinstra, Jr.  
Representative of the Office of the Governor, (unnamed as yet)

A public member (unnamed as yet)

### Staff:

Michelle Zdeb

Kathryn “Kiki” Evinger

### Attendees:

Freda Pepper, Director of Compliance, Keane, Inc.  
Arsene Aka, DOF  
Courtney Stewart, CGO

Jamie Johnstone, DOF  
Kim Gomes, Byrd Group, L.L.C.  
Michael Barlow, Esq., Office of the Governor

The Task Force meeting was brought to order at 1:04pm.

\* \* \*

## INTRODUCTIONS

Senator Townsend, co-chair, thanked the members of the Task Force and the public for attending the meeting. He apologized for not being able to participate in person but stated that he would be participating via conference call. The Senator then turned the meeting over to co-chair Representative Bryon Short.

Representative Short, co-chair, suggested that the members of the Task Force who were present state their names so that Senator Townsend knew who had attended. Representative Short then asked if Senator Townsend would like to make any opening remarks.

Senator Townsend thanked Representative Short. He stated that the Task Force was meeting in Dover due to construction at the Wilmington meeting location, Buena Vista. It is not his intent to have all of the Task Force meetings in Dover. He also notified the Task Force that Thomas Collins, Delaware Bankers Association, was present on the conference call.

## REVIEW OF TASK FORCE TIMETABLE

Representative Short stated that there are currently two other Task Force meetings scheduled. The meetings are on Tuesday, August 12th from 1 p.m. to 3 p.m. and Wednesday, September 10th from 3 p.m. to 5 p.m. Both

meetings will be held at Buena Vista in Wilmington. There will be a fourth meeting tentatively in October but it is not scheduled at this time. The Report for this Task Force is due by November 1, 2014.

## BACKGROUND OF SENATE CONCURRENT RESOLUTION 59

Representative Short asked Senator Townsend if he would like to give any background information about this subject or if he would prefer to skip to the 'Overview of Issues' topic. Senator Townsend said he would like to begin discussing the issues.

## OVERVIEW OF ISSUES

Representative Short began the discussion. He said that it is important to balance the fact that unclaimed property is the third largest source of revenue for Delaware with the State's desire to maintain positive relationships with the companies that choose to reside here. On a more local level, constituents have called him and other State Senators and Representatives to report that they have lost money to the escheat program. The Representative stated that he worked with Secretary Cook, Department of Finance (DOF), several years ago to improve the escheat notification system. He then suggested that the other members of the Task Force, many of whom encounter this issue on a corporate level, state their opinions and observations on the subject.

Senator Lavelle said that everyone on the Task Force understood the importance of escheat and its relation to the State budget. Problems with the escheat process were brought to his and Senator Townsend's attention, resulting in both legislators proposing legislation to rectify the situation by extending the incentive program. Neither piece of legislation was passed, but this Task Force intends to examine the issue in-depth to find a more comprehensive solution. Additionally, Senator Lavelle brought attention to a line in the synopsis of SCR 59 that states that the Task Force seeks to improve the "fairness and compliance of Delaware's unclaimed property program." The key is to find out what the definition of "fairness" should be. He believes that the State and companies may have different ideas of what "fairness" means in this context. The State may be seeking to escheat as much money as possible, while companies may want a shorter auditing period.

Senator Lavelle also questions the fairness of the contracts that the State holds with service providers. He requested that Secretary Cook provide information on the State's history of escheat collection on an annual basis over approximately the past 15 years. The Senator would also like to see copies of the contracts that the State holds with service providers, in order to examine the terms of the contracts. Additionally, he would like to see a record of the legal actions that have been filed against the State relating to this issue. There was an article in *The News Journal* that morning (July 24, 2014) that detailed one such case. He further asked if there were other pending cases and what is the history of the current case. Senator Lavelle noted that he realized that the Task Force includes members with varying backgrounds on this issue and that he looks forward to hearing their views.

Secretary Cook stated that the case discussed in the newspaper that morning was the only such case that has been filed and that he could provide the Task Force with information on that particular case and its history.

Leonard Togman, Esq., public member, retired attorney and partner at Potter, Anderson, said that he agreed with Senator Lavelle that the issue of what constitutes fairness is important. There is a general perception that the auditing process is not fair, particularly the length of time the audit takes and the volume of information requested. These issues make the auditing process onerous. This negatively impacts Delaware's reputation as a good state for states to be incorporated in.

Michael Houghton, Esq., member of the Uniform Law Commission (ULC) for Delaware, said that he represents many Fortune 1000 companies, either in terms of voluntary compliance, companies that are being audited by the State of Delaware or other states, or companies that are a part of Secretary Bullock's Voluntary Disclosure Program (VDA). He thinks that there have been a number of modifications to the statute to address some of the concerns in the corporate community about unclaimed property. The reality of the situation is that there are thousands of corporations that are surprised to find out, after they have been invited to become incorporated in Delaware, that in retain their presence in Delaware they are subject to audits. Audits may or may not be considered aggressive. Companies

should not be surprised to find that they have a legal obligation to file; this negatively impacts Delaware's reputation.

This brings several questions to mind that may be answered during the course of the Task Force. First, does Corporate America believe that they are being dealt with in a fair and transparent way. Second, are there standards and criteria that are understandable relating to an audit. One issue he frequently encounters in his practice that clients find to be unfair is the look-back period that extends to 1981. A ten year look-back period may be more reasonable than a thirty-three year one. Mr. Houghton, in addition to serving on this Task Force, is also chairing a national Task Force for the Uniform Law Commission that is undertaking a revision of the federal Uniform Unclaimed Property Act, which is the law in more than 40 states. The last revision was in 1995. As a result, he is collecting a vast amount of information about this issue on the national level that he would be happy to share with members of this Task Force. This Task Force does not have the time or capacity to do a total overhaul of the Delaware statute. He noted at some point this is an issue that needs to be addressed, since it the Delaware statute outdated.

Mr. Houghton emphasized that this is a delicate issue and actions need to be carefully examined so as not to negatively impact the State. Certain things can be done to promote transparency and consistency, but this is an almost \$600 million per year revenue source for the State, and the risk of consequences to the State's revenue need to be avoided. He does not advise that this process be undone, but some things can be done to make the process more palatable to Corporate America.

Jordon Rosen, Delaware State Chamber of Commerce (DSCC), agreed with many of the comments from previous members, especially regarding improving fairness and compliance. Delaware's reputation is at stake. He would like to see a best practices manual for audits of unclaimed property, both for auditors and for those providing oversight in Dover. Unclaimed property is the third largest source of revenue; scaring away corporations with unclaimed property laws puts this revenue stream at risk. Technology that businesses have today results in companies keeping better records, which leaves the State with less money in an audit. This is a shrinking revenue stream. His fear was that this large level of State revenue is in jeopardy.

Stan Stevenson, Delaware State Bar Association (DSBA), stated he is also a practitioner in the field and is involved in audits. He supported Mr. Rosen's statement because of technology there may not be much that can be done to hold onto that revenue stream. However, there are certain other things that Delaware should be doing simply because they are the right thing to do, including decreasing the audit length and the look-back period. In the last five years there have been improvements that have been made that benefitted the business community and have begun to improve the reputation of the State. Some improvements can also be made in getting property that has been escheated back to the rightful owner.

Representative Jeff Spiegelman asked if the Task Force would directly address some of the issues that have resulted from the Temple-Inland court case, including retroactively applying the 2010 change to State law. He asked if the Task Force wanted to dive into a federal court case. It could be a question for the future.

Senator Townsend answered that it is a topic that he has heard about from others. He said that the Task Force members must be mindful of the litigation and how it overlaps.

Secretary Jeff Bullock, Department of State (DOS), said that it would be helpful to talk about where the Markell Administration is on how this issue is handled, not only as a tax collection issue but as a matter of policy. Most of the comments he heard from Task Force members were about the audit functions. The Administration understands the controversy the audit process has created, including the cost of audits on the holder side and the look-back period. In the course of this Administration there have been conversations with large corporations about how Delaware's audits have affected them as well as about the auditing process's reputational impact on the State. The issue that the Administration has been trying to deal with is how to get more companies into compliance. It is the legal responsibility of companies to be in compliance with Delaware's abandoned property laws. However, how companies meet that obligation, the rules that are in place and what is and is not considered abandoned property are points of controversy. Over the past several years the Administration has tried to move away from a model that relies heavily on audits and towards one that tries to incentivize compliance. That is why the

Administration is focused on this Task Force being about compliance; if companies are in compliance, some problems resolve themselves.

Secretary Bullock stated getting companies into compliance is an issue. In order to pursue this model of incentivizing rather than auditing, DOS has created the VDA, and the DOF have been making reforms. The Secretary noted although it may not seem like it, he believes the model is working. About 550 companies have signed up for the VDA program—three times more than was originally projected. The program has been extended and over \$70 million was collected last year. Once more companies are in compliance, and they are required to file annual reports, the concerns that other Task Force members expressed will be less common. Secretary Bullock emphasized that the Task Force should focus on how to improve corporate compliance with Delaware statutes.

Mr. Houghton stated that one important way to incentivize compliance is to continue audits. He has had clients who received invitations to join the VDA program but refused. He does not have sympathy for these companies if they are audited because the State has set up infrastructure designed to heavily promote coming in on a voluntary basis. The only way people will think that means something is if there are consequences for not joining the program. He thought the audit program is an integral part of promoting compliance; “you have to have the carrot and the stick.”

Secretary Bullock agreed with Mr. Houghton. He compared this situation to the IRS, which was very audit-oriented twenty years ago. It is much less now and it has much more public outreach. However, the IRS still does audits because there is a need for consequences as well as incentives.

Secretary Cook said that part of the job of DOF is to make sure the audit process is fair and equitable. If there is a problem he wants to address it. He wants to hear from members how his department can make the process better. One of the changes that were made to make the process more transparent was, after the property has been escheated, the State sends out due diligence letters informing of the property they have and requesting contact. DOF has reunited over \$100 million with claimants this past year. In terms of revenue, over \$200 million comes in each year as a result of annual collections done by auditors.

Secretary Cook agreed with Secretary Bullock that the Administration’s goal is to incentivize companies to file annually and join the VDA program. This makes annual revenue more stable and predictable. Some companies have ignored invitations to join the VDA program. He questioned why some companies have refused to join and yet are the ones that tend to have the most complaints about the system. Secretary Cook addressed the concern that the look-back period is too long by stating that if companies were in compliance then there is not a long look-back period. He has heard that the audit process has been referred to as “aggressive.” The Secretary stated he is interested in addressing this issue and wants to hear examples of the auditing process being aggressive. The DOF is following the law set forth by the General Assembly. If the law is changed, there could be consequences like Mr. Houghton mentioned.

#### OPEN DISCUSSION BY TASK FORCE

Representative Spiegelman said that the issue of the look-back period is at the crux of the Temple-Inland case. He asked Secretary Cook to explain the case further.

Secretary Cook gave some background on the litigation. He said that the company went through the audit process and DOF requested information from them. Then DOF gave an assessment based on the information that was provided to them. There is an appeals process in place that has been created in the past couple of years that provides for an independent reviewer to come in and hear both sides of the case and make a recommendation to the Secretary of Finance. The Secretary can accept, reject, or modify the recommendation. In this case, the recommendation was that the methodology was correct and a fair audit was done. Secretary Cook accepted this recommendation. The company had the option of appealing to the Court of Chancery, but they decided to sue in federal court.

Senator Lavelle asked to see the report from the previous legislative task force on unclaimed property. He also asked how many companies are there that are escheatable in Delaware, how many have chosen to report, and how many have chosen not to report.

Secretary Cook stated there are over 3,000 that annually report and that there are over one million escheatable companies. He compared it to the gross

receipt tax in that it is a self-reporting system. Larger companies that do not report may be candidates for auditing.

Senator Lavelle asked what Secretary Cook meant by “larger companies.”

Secretary Cook said that if there is a certain segment of an industry where five out of six companies are reporting, the one that is not might be most likely audited. This is a self-reporting process.

Senator Lavelle asked if there is a law requiring companies to fill out forms and submit them to DOF.

Secretary Cook said that there is no such law currently.

Secretary Bullock said that there are some companies that are required to report because they are escheatable in Delaware, but that the amount of escheatable property is so small that it would not be worth the State’s time to pursue an audit.

Secretary Cook said that theoretically if someone had a sub shop that issued a payroll check that was never cashed, that money would be escheatable to the State. However, it would likely be an insignificant amount that the State would not pursue. Larger companies, like Lehman Brothers, would have a larger escheatable amount so the State would be more likely to pursue an audit with them.

Senator Lavelle asked how DOF finds and picks these larger escheatable companies.

Secretary Bullock answered that they research the companies. As a result of the VDA program, DOS has access to the records of who is and is not in compliance with DOF. They look at the top 2,000 corporations in the world to see if they are in compliance. These companies are a good place to start because they are large and the chances that they do not have a lot of reportable escheatable property are small. The DOS sends out hundreds of invitations to participate in the VDA program. About 25% of those companies are participating in the program but, as Secretary Cook mentioned, that means that about 75% of the companies are not participating. These are very large and famous companies.

Senator Lavelle stated that it would be helpful if Secretary Cook could provide more information about what rate of returned claims is, as well as any other programmatic issues of DOF. This might be helpful for members who were not present at the last Task Force (2005) addressing this issue.

Mr. Houghton stated that unclaimed property is like a finite natural resource. He explained there are companies that have been in business for 20-50 years. In Delaware the law is that the first instance of unclaimed property must be reported to the state of the last known address of the owner of the property. If a company is incorporated in Delaware but operates primarily or exclusively in another state, Delaware still has a legal right to the unclaimed property. This is a frustrating issue for corporate owners. Unless federal law is changed, the state of incorporation has a right to the unclaimed property. Periodically the federal law is challenged and there is a threat that the state of incorporation would get nothing.

Representative Spiegelman asked if that was a potential outcome of the current Temple-Inland litigation.

Mr. Houghton said it is a potential outcome. Additionally, there is other pending federal litigation that he is involved in with the Attorney General’s office that sues about 30 nationally known Delaware corporations. The litigation alleges that the companies committed fraud by not reporting their unclaimed property. The State is now dealing with a constitutional assault on the Delaware unclaimed property law as a result. Mr. Houghton recommended that the Task Force keep track of this case as it plays out in Delaware federal court because the results of it could have serious implications for the Delaware franchise. Eventually this “natural resource” of unclaimed property will run out as the State audits all of the large corporations in Delaware.

Mr. Houghton echoed Mr. Rosen’s point that technology advances will also contribute to the drop in state revenue as companies start to have better record-keeping. They will want to avoid having their unclaimed property estimated for years that they no longer have records, since most companies do not keep records for over 30 years. The majority of the liability in audits is from estimated records, which corporations do not like because the estimated liability can be significant. Mr.

Houghton questions what the State should do when the revenue stream dries up.

Secretary Cook stated that if a company goes through the estimation process there is something called “owner unknowable” property. The State gets the majority of its money from following the Secondary Rule (without address the property is escheated to the state of incorporation) of the Supreme Court. Secretary Cook suggested that the DOF give a presentation and Power Point that delves into some of these issues and that clarifies the auditing process. However, if there is a complaint, it is important to remember that it is the State that runs the audit, not the auditing company. If there is any problem it falls back on DOF. He also reiterated his earlier request to hear from companies if DOF is being aggressive in its auditing process and to provide examples. He suggested that those companies make a presentation as well.

Mr. Togman said that there was a prior Task Force (2005) that considered this issue. At that Task Force, they invited people in the industry to come in and explain the problems they are facing with the system. He suggested that extending that invitation again for industry members to testify before the committee would be beneficial.

Representative Short asked Mr. Togman if industry members responded favorably to that invitation and came to testify.

Mr. Togman said that they did respond favorably and that a large number attended.

Mr. Houghton said that he noticed that Secretary Cook was understandably reacting to the word “aggressive.” He said he did not believe that the members of the Task Force were using “aggressive” to mean that Delaware or its auditors are unprofessional, personally offensive or berating companies. He thought they used the word to describe the tools that are used to implement the program, such as the look-back period and estimated liability. Companies do not have as much of a problem using seven years of records to estimate the previous seven years as they do seven years being used to estimate 25 years of liability. The appeals process is also concerning because it is convoluted and antiquated. It has an independent reviewer who is appointed by the Secretary of Finance and it is the Secretary of Finance

who approves or rejects the result. Mr. Houghton said he understands the process, but nationally the system is criticized because it is seen to be a circular process. He agreed that outside groups and companies should be invited to make a presentation to the Task Force about their concerns. He suggested finding someone willing to represent and speak with one voice on behalf of these groups.

Secretary Bullock agreed that the appeals process may need to be reviewed and updated, though it has only been utilized once. However, it has been almost 20 years since *Delaware v. New York* (1996). Companies have had all that time to come into compliance, meaning that their look-back would not have been as long. If they had come into compliance in 1996 their look-back would have only been ten years. They chose to wait.

Mr. Houghton stated there is only one other state, California, that has a look-back period as long as Delaware’s. All other states have one version or another of the Uniform Law.

Secretary Bullock noted he wanted to make sure that the laws are not incentivizing illegal activity.

Mr. Houghton said that other states commence a series of audits over a shorter period of time so that the process is not dragged out. It prevents the running of the statute of limitations. An audit can be initiated as a sort of placeholder for a fuller review. States have agreed to this shorter look-back period but in return have increased their audits. No one should get a free ride. The State could consider giving companies a shorter look-back period but then make reporting unclaimed property a stronger requirement. This would tell companies that they cannot have it both ways; if they want shorter look-back periods and greater fairness then they should have to comply with reporting laws.

Representative Spiegelman asked Mr. Houghton that if the look-back period was reduced to fifteen years but the likelihood of a State audit was much higher if that would more quickly deplete the revenue stream. There would be a spike in revenue but it would fall more quickly. Representative Spiegelman wondered if this would be almost a lose-lose situation.

Mr. Houghton answered that he does not think that there would be a spike in revenue because the

period of review would be cut by more than 50%. He thought that it would actually level off. There are still a lot of companies left to audit and auditing is a time-consuming process. He agreed that it may be a lose-lose situation for the State, since the revenue will eventually run out in any case.

Senator Lavelle asked if there was a statute of limitations on this issue.

Mr. Stevenson answered that there is a statute of limitations but the company has to file a return in order to be entitled to it. He said that it is similar to a standard state tax limitation, where how far the look-back is depends on if there is a substantial understatement and if taxes have been filed in recent years. The problem in his opinion is that large corporation could flood offices with \$0 returns. He was not sure if there was a mechanism in place that could handle that many returns from that many companies.

Representative Spiegelman stated that there were a lot of aspects of this issue that he was not aware of. He asked Secretary Cook who he should talk to in order to get more information on the issue.

Secretary Cook said that he would be willing speak with Rep. Spiegelman. He said his office is willing to sit down with individual members to explain the details of the issue, in addition to the presentation that he will be giving the Task Force. He also suggested that he could make the actual auditors available to answer questions about the work that they do.

Senator Townsend said that he appreciated Secretary Cook being willing to sit down with members individually to answer their questions. In terms of the presentation, he said it could be done as part of the formal agenda of the Task Force or it could be distributed to members informally for them to review. Distributing the presentation informally could leave the Task Force with more time to consider other issues.

Mr. Togman said he agreed with Senator Townsend. At the last Task Force (2005) the State gave a presentation on their views and the industry gave a presentation with their comments. He thought it would be invaluable to the Task Force to hear both sides as a formal part of the Task Force meeting.

Senator Lavelle suggested that the presentation on the history of the issue could be included in the report.

Representative Spiegelman agreed with Senator Lavelle.

Mr. Houghton stated that it would be useful to ask interested constituencies to submit in writing their views on the issue for the Task Force to review. This would save time since it would not spend time covering the basics. He said that the ULC has come to the conclusion that auditors are a very necessary part of the process. Rules can be made, however, dictating what the role of the auditors should be, how many there should be, etc. A small number of auditing firms collectively handle up to 80% of these auditing cases. An argument could be made that the work should be spread around companies more easily, especially if there are native Delaware firms that would want to be involved in the process.

Secretary Bullock stated that because Delaware is a small state, hiring Delaware firms would likely end up causing a conflict of interest for him.

Representative Short reiterated Secretary Cook's point that it is critical that the Task Force hear about specific issues from the people involved in the industry.

Senator Lavelle said that the State has very large contracts with certain auditing companies. He asked if this caused an increase in competition. There may be a better deal for Delaware taxpayers. He also asked how DOF decides which companies to use and why Kelmar seems to be getting most of the business.

Secretary Cook said that the DOF has contracts with six entities that do this work, but others can submit applications to be considered for the job. DOF does look at what areas particular companies have experience auditing in when DOF decides which company to use. DOF has been looking to make sure that they spread the work around to multiple companies. Kelmar has supported the spreading around of the State's business, but the other companies are much smaller than Kelmar and may not be able to handle the same volume of work.

Secretary Bullock said that Kelmar has contracts with forty other states. If Delaware decides to give them less business it won't hurt them very much. They have diversified so much that they could not handle all of Delaware's audits even if they wanted to.

Mr. Houghton stated that even though Kelmar operates in forty other states, there are no other states in that group that generate as much revenue as Delaware does. In certain areas certain firms have expertise and that is why the work flows to them. The Task Force can investigate what it can do to encourage more capable auditors to work for the State.

Senator Lavelle asked for the names of three other service providers.

Mr. Houghton named Specialty Audit Services (SAS), Kelly Innovative Advocate Group, and Unclaimed Property Clearinghouse (UPCH, a Xerox subsidiary). In the past few years there have been a proliferation of other service providers.

Secretary Bullock commented that these smaller companies are often not capable of auditing a large Fortune 500 company.

Senator Lavelle asked how many of the companies in the Fortune 500 or Fortune 1000 are not in the program.

Secretary Bullock answered that a pretty significant number are not.

Representative Spiegelman asked if the State could ideally move towards using multiple smaller companies instead of fewer large companies if that would promote the idea of fairness.

Secretary Bullock said yes.

Secretary Cook said that DOF is not adverse to this idea, but that smaller firms may get overloaded and the audit process may take longer.

Representative Short stated that the House of Representatives is still pursuing the nomination of a House member of the public. Michael Barlow is also filling in for the Office of the Governor as they are awaiting an appointee as well.

## PUBLIC COMMENT

Representative Short asked if any members of the public wanted to comment on this issue.

Kim Gomes, Byrd Group, LLC., said that she was present at the meeting on behalf of many clients, including the Council on State Taxation (COST). She stated that this issue is something that has garnered national attention. She offered to give Secretary Cook examples of what she would consider “aggressive” auditing behavior. COST would be happy to come in to testify. Since there is not a lot of time to examine this issue, she requested that the public comment period be continued and that members of the public be allowed to address the Task Force.

Mr. Togman commented that if members from the industry are invited, it may be difficult to get them to testify because they are concerned that if they have complaints they will get adverse reactions to their audits from DOF. Some were reluctant in the previous Task Force (2005) to testify.

Secretary Bullock said that he met with the Executive Director of COST about their concerns. He noticed that most of their complaints were historic and fewer were recent. He said it may be more valuable if the issues that industry members present are focused more on the present since Secretary Cook has done a lot of work to reform this area in the past several years.

Mr. Houghton said that he was also a member of the original Task Force (2005) and remembered the reluctance of some industry members to testify. He suggested one way to address the issue would be to invite the trade organizations to be the spokespeople for the industry. He also acknowledged the Division of Revenue’s reforms in the past several years as being very positive changes. He does not believe that this Task Force will complete an overhaul of the unclaimed property law, but will instead address a shorter list of specific issues from the holder community and the State.

Representative Short thanked the Task Force members for attending and for their comments.

The meeting was adjourned at 2:31 p.m.

# Minutes of the Meeting of the Unclaimed Property Task Force of Tuesday, August 12, 2014

Buck Library, Buena Vista State Conference Center, 1:00 p.m. – 3:00 p.m.

Meeting Attendance: Task Force Members Present:

Senator Bryan Townsend  
Representative Jeff Spiegelman  
Secretary Thomas Cook  
Thomas Collins  
Edward Ratledge (newly-appointed public member)  
Leonard Togman, Esq.

Senator Greg Lavelle  
Secretary Jeffrey Bullock  
Controller General Michael Morton  
Michael Houghton, Esq.  
Jordon Rosen  
Robert Tuinstra, Jr.

Absent:

Representative Bryon Short  
Representative of the Office of the Governor (not yet named)

Stan Stevenson, Esq.

Staff:

Michelle Zdeb

Kathryn “Kiki” Evinger

Attendees:

Jamie Johnstone, DOF  
David Gregor, DOF  
Caroline Cross, DOJ representing DOF  
Rick Geisenberger, DOS

Arsene Aka, DOF  
Courtney Stewart, CGO  
Bob Byrd, Byrd Group, LLC.

The Task Force Meeting was brought to order at 1:12 p.m.

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## INTRODUCTIONS

Senator Bryan Townsend, co-chair, thanked the members of the Task Force and the public for attending the meeting. He confirmed that Senator Lavelle and Michael Houghton, Uniform Law Commission (ULC), would be participating via conference call. The Senator then asked the members of the Task Force and the public to introduce themselves and state the organization they were representing.

## PRESENTATION BY DEPARTMENT OF FINANCE

Senator Townsend turned the floor over to Secretary

Thomas Cook, Department of Finance (DOF).

Secretary Cook, Department of Finance (DOF), said the presentation would provide the Task Force members with information on how the unclaimed property area works. The Secretary noted in the future, there will be presentations from the advocates for the holders as well as some of DOF’s auditors. He then introduced David Gregor, Deputy Secretary of Finance and State Escheator, as he would be giving the presentation. Secretary Cook further noted he would be happy to answer any questions Task Force members have about the presentation.

Deputy Secretary David Gregor noted the presentation will focus on the enforcement part of the audit process. He would be happy to discuss other aspects of the process if the Task Force has questions about specific aspects. He then began the presentation.

Deputy Secretary Gregor stated that the business does not own the unclaimed property. The holder has no legal right to the property. These types of unclaimed property laws are not unique to Delaware; all fifty states have some sort of unclaimed property laws. This is a complicated issue, but the Deputy Secretary emphasized that the most basic fact of the issue is that the money does not belong to the holders.

The basic purpose of unclaimed property programs is to reunite the rightful owner with their property. If an owner is unable to be found, that property should be used for the public good. The State Legislature determines what is considered a “public good” through the budgetary process. Holders should not be unfairly rewarded by claiming the true owner’s property. This decision to use unclaimed property for the public good if no owner can be easily found has been confirmed with multiple U.S. Supreme Court (SCOTUS) decisions.

DOF would like to see more voluntary compliance with reporting unclaimed property. In order to encourage voluntary reporting, Delaware has engaged in education and outreach. There have been several public-private task forces aimed at addressing problems in the field. There is a uniform reporting format between all fifty states and the Delaware SOS Voluntary Disclosure Agreement (VDA) adopted in 2012, which allows for perpetual amnesty. The Deputy Secretary noted this is very business friendly. Despite all of these efforts, most states, including Delaware, only have voluntary compliance percentages in the single digits. There are hundreds of thousands of entities in the State of Delaware and only 3,500 – 4,000 of them file each year. Compliance is definitely an issue DOF is dealing with.

Delaware needs a healthy enforcement program because it is necessary to increase voluntary compliance. If there is no threat of an audit there is no incentive to enter the VDA. Deputy Secretary Gregor referred to a handout provided by DOF titled “Escheat Breakdown: FY 2000 to FY 2014.” He noted that in FY’s 2000 – 2002 the State’s Average Cash Annual Filings were \$87.4

million and Average Enforcement was \$45.7 million. It was around this time that DOF started having an employee, with an auditing background, working solely on unclaimed property rather than having several employees split their time between other fields in DOF. This led to a steady increase in annual cash filings and enforcement, with Delaware’s FY’s 2012 – 2014 Average Cash Annual filings at \$249.7 million and average enforcement \$175.8 million. He did not think that this would have been the case if Delaware had eliminated or reduced its enforcement program. States that discontinue audit programs have seen decreases in voluntary compliance. Noncompliance puts businesses that do comply at a disadvantage, since they are spending time to report to DOF, and that is unfair. Enforcement is a necessary component of any audit process.

In most instances, states do not have the resources or expertise to engage in complicated audits that involve multi-state entities. Contractors have filled that void. States have used contractors in the audit process for thirty years. Contract examiners allow for multi-state audits, which reduce the administrative burden on holders. Holders often seek a “global settlement” so that they are completely audited only once.

The role of the contractor is limited to the examination of the holder’s books and records. Only the State selects the holders to be examined, and they are engaged throughout the entire process. Contractors cannot initiate an audit. The State resolves all contested issues during the exam, maintaining daily contact and making monthly reviews of all cases. The State encourages holders who are having difficulties with contractors to contact the State to resolve the problem. The State alone makes the decision regarding final liability. The contractor makes a recommendation but the State makes the final call; the contractors are not involved at all in making the final decision.

Delaware is not unique in its use of contractors. All states use them. With one possible exception, all states employ some element of contingency format in their billings. DOF has received two main criticisms about contractors. The first is that contractors are “aggressive.” This criticism lacks specificity and supporting examples of contractors behaving “aggressively.” Contractors can only operate under the laws that are set by the State and the State makes all final decisions. DOF is interested in hearing specific examples of instances when contractors

behaved aggressively.

The second criticism is that because there is a contingency fee that it is believed that contractors “inflate” assessments. Contractors produce findings based on an examination of the holder’s actual books and records. The State alone makes the call on the amount of an assessment and on holder remediation. In terms of estimation, Deputy Secretary Gregor said this is an issue of fairness. If a company turns over the required records then estimation is not necessary. If they do not, whether because they no longer have the records or they refuse to turn them over to the State, then estimation is necessary to complete a fair audit.

Secretary Cook asked Deputy Secretary Gregor to explain more about how base years are chosen to base an audit on when estimation is necessary.

Deputy Secretary Gregor said it is necessary to have data to base an audit on. Depending on the scope of the look-back, it is necessary to have base years that best reflect the activities, procedures, and accounting policies of a company during the years that are being estimated. It is not uncommon for DOF and the holder to have a negotiation over base years. The holder may want certain years to be used as the base years because they know that they implemented a new accounting system shortly prior. The State may feel that, because the look-back period extends to 1986, that an earlier set of base years would be more indicative of the state of the company during the years that records are not available. This is a negotiation and no two holders are the same.

Secretary Cook wanted to emphasize that this process of determining base years is a negotiation. There is a discussion between the State and holders.

Leonard Togman, public member, retired attorney at Potter Anderson, asked what DOF would do if there were no records at all available for earlier periods in a company, if only very recent records were available.

Deputy Secretary Gregor answered that if that was the case then the State would have to use the most recent records as a base period. He said that Michelle Whitaker, DOF Audit Manager, (not present) would have a better sense of what would be done in that situation and he offered to note Mr. Togman’s question and get back to him.

Robert Tuinstra, Jr., Delaware Business Roundtable (DBR), asked how many years back the State is looking in this type of audit.

Deputy Secretary Gregor answered that the look-back period goes to 1986.

Mr. Tuinstra asked for clarification that the State was looking for a transaction from that period in order to find if there was an error. He then asked what level of record the state was looking for.

Deputy Secretary Gregor stated that finding an error would be the reason the State was looking back in that time period. He said that often the State would be looking for checks and invoices. If a company does have records from every year from 1986 to present then the contractor would utilize a sampling method so that every single document does not have to be reviewed. A sample from the whole would be taken and the State and holder would agree that, within a 5% margin of error, it would be representative of the company’s history.

Mr. Togman asked if the State would ever use an outside arbiter if there was a disagreement between the State and the holder.

Deputy Secretary Gregor said he did not think so. During the long process of the audit there is a lot of give and take between the State and the holder. These types of disagreements tend to come at the end of an examination.

Caroline Cross, Esq., Deputy Attorney General representing the Department of Finance (DOF), attending as a member of the public, stated that there are times when there is a disagreement. However, both sides realize that the cost of pursuing external arbitration is usually greater than the amount of property that is causing the disagreement.

Representative Spiegelman asked if the amount of time it takes to complete an audit is contingent on the size of the company or if there was an average amount of time.

Deputy Secretary Gregor said that the length of the exam usually depends on how long it takes companies to produce records rather than the size of the company. Negotiations over the sampling and the base period also

take time. Other times companies refuse to cooperate or do not have an accounting process.

Secretary Jeff Bullock, Department of State (DOS), added that the complexity of the company also influences the amount of time an audit takes. In some cases, a company may have acquired other companies since 1986. Each company may have used a different accounting system before being acquired, which makes reviewing records more difficult.

Deputy Secretary Gregor stated that there is a process called “scoping” that is used in this type of situation. If a company has subsidiaries that are primarily located in another state and that do not have a Delaware charter then the audit might not examine that subsidiary because there is a low likelihood that Delaware would be entitled to any property. Any subsidiary that operates in Delaware or that is incorporated in Delaware would be of interest to the audit.

Representative Spiegelman asked if this could be a multi-year process.

Deputy Secretary Gregor said that it could. It is not uncommon for the holder to change representation or advocate which would slow or speed the process. This is a complex process that takes time. Approximately 80% of the holders cooperate with the audit process.

Mr. Houghton said that in his practice the length of audits has extended considerably over the past decade. Most audits he used to participate in took between 18 months and two years to complete. Many audits now go well over three years, sometimes taking up to four or five years. He did not think the reason for this was because of the complexity of the company or unwillingness to participate on the part of the holder. He said that there are so many audits in progress currently that the audit department may be overwhelmed and therefore be unable to complete audits promptly.

He asked if the Division of Revenue has any views on how to expedite audits and if they have any statistics related to the average length of audits.

Deputy Secretary Gregor said that he did not have any statistics readily available to confirm the length of audits. If it is true that audits are taking up to five years because DOF is overwhelmed, then he would

be interested in investigating that issue and gathering data on it. There is a perception that the State is too aggressive in these audits. The State does have means to compel a company to release information related to the audit, such as issuing a summons or going to court, but the State has been reluctant to use these means because it did not want to be thought of as aggressive. However the DOF is rethinking this strategy because they are being called aggressive anyway.

Secretary Bullock said that the length of the audit is a very important issue. Before DOS started the VDA program, Secretary Bullock called the companies who had been unhappy in the past with their audits. He spoke with the CFO of a large Fortune 500 company who said that if the State cannot complete audits within a year that they are doing something wrong. He agreed. When the VDA program started, the goal was to complete audits within nine months. He was told by members of the financial community, including some members of this Task Force, that this was an unrealistic goal. Within the first few months of the program he realized they were right.

One of the first changes DOS made to the law was to allow them more time to complete an audit. Some things sound great in theory but do not work in practice. The capacity of the State, holder, and people who work for the State and who work for the holder to complete the work must be considered. VDA's now take about eighteen months. Because there is a large amount of work to be completed in that timeframe, DOS is putting people on schedules to make sure the work is completed on time. There are some companies who are an exception and complete their audit in nine months, but this is not the norm. Sometimes the CEO's prioritize the audit and it gets done faster, but most of the time it is not prioritized.

Representative Spiegelman brought up the question of “fairness” that was discussed at the previous meeting. He asked if increasing the number of audit firms would help solve the issue of fairness as well as reduce the amount of time it takes to do an audit.

Secretary Bullock agreed it would, but said that the length of time is not solely dependent on the State but also on the holder and the people they have working for them. That is a finite population as well and they are overworked. It is necessary to look at capacity throughout

the process, not just on the State's side of things.

Edward Ratledge, public member, Director of the University of Delaware's Center for Applied Demography & Survey Research (CADSR), asked about the sampling process for the look-back period Deputy Secretary Gregor referred to in his presentation. He asked if larger companies required more complicated sampling methods. He questioned whether these more complicated sampling methods and larger sample sizes increased the risk for error and inflation.

Deputy Secretary Gregor answered that the contractors they hire use stratified samples. Within the strata they are making an estimate of the mean and the standard deviation. A larger standard deviation results in a larger mean and heavier sample. In some audits, there are some strata that have extreme outliers that have to be more closely examined. They do a 100% sample on those outliers and then as the amounts get lower and the standard deviation gets tighter there can be a lower sampling rate. This process does take time.

Deputy Secretary Gregor continued with his presentation. Delaware does not use a straight contingency model. They had used an hourly model in the past, but holders complained that the examination was being dragged out to inflate billable hours. The State also made payments and did not always see results. Currently, Delaware uses a hybrid model of an hourly rate up to a percentage cap. This model guards against both complaints of running up hours and inflating findings. The cap saves the State money. The hourly rate is based on rates that the Big-4 accounting firms were receiving, though with a discount then applied.

In 24% of cases there are no findings; the holder owes the State nothing. This could be because the holder is entirely in compliance or because they have gone bankrupt. If the State used only a straight hourly model then there is no incentive for the contractor to close the case. In a straight contingency model, if it looks like there will not be any findings the contractor would receive nothing; they could possibly decide to cut their losses and move on to another more lucrative case without finishing. The hybrid model protects against both of these scenarios in those 24% of cases where there are no findings.

Mr. Tuinstra asked if the contingency model was

based on the findings or the ultimate resolution.

Deputy Secretary Gregor answered that it is based on the ultimate resolution. Kelmar will be presenting at the next Task Force meeting and will be able to discuss this issue further. They are comfortable with the State making the final call on audits.

Mr. Togman asked for clarification that in cases where there are no findings, contractors are paid for a straight hourly audit.

Deputy Secretary Gregor said that is correct.

Mr. Houghton asked how many audits result in zero findings. He has been working in this field for over twenty years and knows of only one time that has happened.

Deputy Secretary Gregor answered that Kelmar reports that in their audits, they receive zero findings results 24% of the time.

Mr. Houghton asked if they were specifically zero findings or if there was some other basis for there being no finding of liability, like the company had gone bankrupt.

Deputy Secretary Gregor agreed that it could be many factors that caused the zero findings, including bankruptcy.

Mr. Houghton asked how many states have contract auditors that have contracts that are the length of time that Delaware's have, which could extend from five to nine years.

Deputy Secretary Gregor said he did not know the answer to that but would be happy to get further information about the contracts Delaware auditors sign. Since the auditing process is so lengthy, it is necessary to have longer contracts so that the contract does not expire in the middle of an audit. Contractors would be able to walk away from an audit and then the State would have to start from scratch on that audit. This would be unfair to the holder as well who will have sunk time and money into the audit already.

Mr. Rosen asked if the contractor is responsible for audits dragging out. He asked if DOF has considered

a periodic review of audits to see if contractors tend to drag out audits that have smaller findings to get a greater hourly rate. He also said that consulting is a business that generally charges \$175/hour. When the State uses the hybrid model they pay them \$150/hour up front. When the audit is settled they get paid 12% of a diminishing percentage over a certain threshold. Some of the hourly contracts are \$495/hour. Deputy Secretary Gregor had explained that this is based on the rates the Big-4 accounting firms charge, but Mr. Rosen said that those firms are not average accounting firms in Delaware. Most firms are much smaller and charge much less. He asked why the State is paying so much for these services.

Deputy Secretary Gregor said that they do not think that the contractors are dragging audits out. He said it was important to understand that the unclaimed property audit does not proceed in lockstep. The State is working on several different aspects of the audit at the same time, such as payroll, accounts payable, and securities. Often, lots of progress will be made on one aspect while there may be disputes in others that hold up the process.

Ms. Cross agreed that this was the case. She has attended several of Ms. Whitaker's monthly meetings with contractors and says that she and her team examine the progress being made very thoroughly. It would be very difficult for contractors to drag the process out without Ms. Whitaker noticing.

Deputy Secretary Gregor said that in regard to Mr. Tuinstra's other question about why the State is paying so much for these services, there are a lot of people involved in the process and there are few people who are experts in the field. Only certain people have this expertise and a good reputation. It is a niche market.

Deputy Secretary Gregor returned to his presentation. He confirmed that the reason that contracts with contract auditors are so long is because unclaimed property exams typically take years. A shorter contract length would mean renegotiating payment with exams only partially complete. The cost is locked in but operations are not. The State can stop assigning cases or reassign cases from a particular contract auditor at any time.

The State is responsive to the business community

and this issue is important to the State as well. The DOF has participated in two previous task forces (2000 and 2006). The appeals process was also developed to benefit the business community. DOS has implemented the VDA program which has been successful with over 550 companies in compliance. The fact that the State is responsible for audits and overseeing contractors will not change; the State makes all critical decisions in the examination process. The reason the rate of returns is lower than in other states is because the SCOTUS has upheld that in cases of owner unknowable property, the state of incorporation can claim it. In the last year, DOF has made great strides in reuniting unclaimed property with owner, including increasing due diligence letters. In FY 2013, the State collected \$191.7 million under "Extraordinary Items."

Representative Spiegelman asked why there was such a large increase in the equity processing between FY's 2013 and 2014.

Deputy Secretary Gregor said that this occurred because in FY 2013 there was no equity processing done. Around that time was when DOF increased their due diligence, but they could not process them all at once. They also started doing a better job processing claims. There has been an increased focus on customer service: \$104 million was returned to owners in FY 2014 claims.

Senator Townsend asked if the fees paid to Kelmar were listed under "Operating Expenses."

Deputy Secretary Gregor said yes. Prior to FY 2011 the DOF had statutory authority to take the net of what contractors gave them for any type of abandoned property. The property escheated was put into a custodial account and the contractors took their share and left the rest for the State. Annual internal review of DOF records resulted in DOF now listing this as gross revenue.

Senator Townsend asked how easy it would be to extrapolate backwards to find out how much money was paid to contractors in years before it was required to be reported.

Deputy Secretary Gregor said that they have done that.

Senator Townsend asked if it would be easy to put

that in a spreadsheet similar to the “Escheat Breakdown: FY 2000 to FY 2014” that the Task Force was examining.

Deputy Secretary Gregor said that it could be done and that he would provide that information to the Task Force members.

Jordon Rosen, Delaware State Chamber of Commerce (DSCC), asked if the State regulates people who want to charge a fee for finding unclaimed property.

Deputy Secretary Gregor said that one of the reasons that DOF likes working with contracting companies like Kelmar is that their only job is as a contractor; they do not represent other parties at all. There is no blurring of lines. Some firms may advocate for states and holders at the same time. DOF has no official position on those firms that represent more than one interested party.

Ms. Cross said that there is no statute regarding this type of business practice. DOF receives weekly requests from finders asking DOF to divulge information related to finding unclaimed property to use for a profit. There are very strict confidentiality rules and this information is never turned over to them. DOF does its best to protect owners from this type of predatory practice. The State does not charge a fee to unite unclaimed property with owners.

Mr. Togman asked what made the State start paying out claims.

Deputy Secretary Gregor said that the State has always been paying out claims. However, when the State realized it was not adequately performing its due diligence, it sought to rectify that by increasing notification for owners of unclaimed property. Over 160,000 pieces of mail were sent out to notify owners. This is now standard practice.

Mr. Togman said that for several years when people’s names were published in the newspaper notifying them of their unclaimed property, including his own, that when they submitted the required forms they got no response.

Deputy Secretary Gregor said that he apologizes if that was the case. There was a backlog and things were not being done as efficiently as they could have. They have made significant administrative changes in

order to improve service. Currently they are trying to update their technology to allow forms to be submitted electronically in PDF form.

#### OPEN DISCUSSION BY TASK FORCE

Mr. Houghton made several comments. Firstly, one of the recommendations that came out of the 2006 Task Force Report was to examine the means of the Division of Revenue, including salary level and staffing, to try to enhance the internal capacity to use internal staffing to improve productivity rather than contracting the work out to contingent-fee contract auditors. He thinks this is something that this Task Force should reexamine.

Secondly, Mr. Houghton said that it is his understanding that Kelmar is now representing over forty states and is increasing its commitment to states. Kelmar is dedicating significant resources to serving these states. Mr. Houghton thinks that there is a connection between this increased workload for Kelmar and the increase in the amount of time it takes for them to complete an audit. This amount of work they have for other states may be impacting the work they do for Delaware. He asked if the DOF agrees that there is a correlation.

Thirdly, Mr. Houghton addressed Secretary Cook’s earlier comments regarding auditors being described as “aggressive” and his interest in hearing about specific examples of auditors behaving in this manner. He said he does not think that there is any one particular incident. When holders call auditors “aggressive” Mr. Houghton believes they are referring to aspects of the auditing program, such as the long look-back period and the estimation process. The labeling is a broad critique of the entire Delaware audit system. He asked what the DOF’s position was on shortening the look-back period.

Deputy Secretary Gregor said in regards to Kelmar and the expanding scope of their business, he did not believe that an increase in the number of states they are serving is impacting their business. As they have taken on more states as clients they have expanded their business and increased the number of people working for them.

In terms of the 2006 Task Force Report, the previous chairperson was defeated in an ensuing election. This

could have contributed to the report not being widely distributed. A lot of resources shortly after the report was released were geared toward internal control and regulation. The Great Recession came shortly after that, which slowed reform down even more. Hiring was frozen in all State agencies. This is why the State had to contract work out rather than hire more people to do the work internally. Now more people can be hired but the department has to decide the best way to utilize them. Additionally there is the fear that DOF will hire more people, take two years to train them, and then they will be lured away by one of the private auditing firms who offer higher salaries. It would be a lost investment for the State. It is an issue worth talking about and DOF is interested in hiring more people, but this situation is a potential reality that has to also be considered.

Representative Spiegelman asked if in a perfect world where DOF would be able to hire all the people it needed, if there would be an increase in the gross amount to the State because the State would be able to address more backlogged cases or will cases just be handled internally a little more easily.

Deputy Secretary Gregor answered that in-house people would not be the people who would be assigned to the large interstate cases. DOF would assign those to regional contractors.

Representative Spiegelman asked if this would be difficult to sell as an investment.

Deputy Secretary Gregor said that it probably would be.

Secretary Cook remarked that there are people who ask for this expansion of the department who at the same time oppose the expansion of government; it is a double edged sword.

Senator Lavelle said that a case could be made to promote efficiency overall, to incentivize employees to work for the State and to stay. This would save the State a lot of money. Senator Lavelle said that the 1981 look-back period was very aggressive and was out of step with other states. He asked whether any study or analysis has been done to examine what the effect on revenue would be if the look-back period was significantly reduced.

Secretary Bullock said the more important question

is if someone could quantify how changing the look-back period was going to improve compliance. The VDA program offers a shorter look-back period and 2/3 of companies still have not signed up. Changing the look-back period seems to have had no impact.

Mr. Togman stated that 30% sign-up to the VDA is still somewhat successful.

Senator Townsend remarked that it would be difficult to find out if the companies joined because of the decreased look-back period or for some other reason.

Mr. Tuinstra said that one of the issues around perceived fairness is the look-back period. One of the reasons that companies are more compliant with tax than with unclaimed property is because there is a well-known and well-defined look-back period that is shorter. Companies maintain their records in preparation for a possible audit. The unclaimed property look-back period covers more than twenty years; finding records that old is next to impossible for companies. Companies are trying to defend against the extrapolation of data, but they need to have records to support their version of the extrapolation. They are often not expecting such a long look-back period and Corporate America does not usually keep transactional-level data that old.

Mr. Rosen said that he remembered in the previous meeting that the Division of Revenue said that they did not want to be flooded with tons of \$0 filings. Some companies have the perception that if they do not have escheatable property then they do not have to file. When they do file their escheatable property they are surprised with an audit. They do not realize that they should have filed every year regardless of whether they had any escheatable property. With no filings there is no statute of limitations and they are suddenly required to produce twenty plus years of records when the standard for record keeping is only about seven years. This is a question of fairness of the process.

Mr. Rosen agreed with Secretary Bullock that there may be no connection between the length of time of the look-back period and compliance. However, he said the State should make it as easy as possible for companies to comply. He asked why the State does not consider including an unclaimed property line on the annual franchise tax form. That would give businesses a sense

of certainty that the three year statute of limitations would start. It would be done electronically so that the DOF would not be inundated with forms. Alternatively, it could be added to the business entity tax return. There are some difficulties associated with this, but the idea is to make it easier for companies to report and be certain that there was a shorter statute of limitations.

Mr. Tuinstra agreed with Mr. Rosen. In the tax world, you file a \$0 return because you want the statute of limitations to start, which is the protection. It should be the same way in unclaimed property. There is always a question of whether a company is underreporting or is not filing, and Mr. Tuinstra said he has no problem with extending the statute of limitations if that is the issue, but it should be clear what responsibilities companies have with regards to keeping records and filing.

Secretary Bullock said he agrees that the process should be easier. However, DOS is not a tax collection agency so the methods Mr. Rosen described would not be the right mechanism. A lot of companies do not have a \$0 return. They are simply not meeting their requirements under the law. If they had come into compliance 15 – 20 years ago they would not have as long of a look-back period.

Mr. Tuinstra said that he has no sympathy for a non-filing company that is deliberately playing the audit lottery.

Secretary Bullock said that the companies that are being targeted for auditing are large companies that are deliberately not filing and that there is a greater chance of escheatable property being collected.

Mr. Tuinstra said that not all the companies the Task Force will hear from may fall in that category.

Deputy Secretary Gregor said that one of the things he wants to emphasize is that contractors only audit the companies the State tells them to. They only operate within the policies and statutes that the State allows. Contractors did not create the look-back period. If holders are unhappy with the look-back period they should direct those complaints at the State and not at the contractors.

Secretary Bullock stated that he has no problem reducing the look-back period. He is focused on

increasing compliance.

Mr. Rosen said that he believes if companies deliberately do not comply, they need to accept the consequences. However, the State needs to make sure that holders know what their responsibilities to the State are in terms of filing and to make it as easy as possible to file.

Senator Townsend asked if other members of the Task Force wanted to respond to a point Mr. Rosen made earlier regarding holders being lured into believing that they do not have to file. He did not recall hearing that being the case.

Mr. Rosen agreed that he would like a response to that question since it is a very troubling idea.

Secretary Cook said there is no penalty for filing a \$0 unclaimed property return.

Senator Townsend asked if there were instructions given telling companies not to file if they have a \$0 return, which leaves the statute of limitations open for them.

Mr. Tuinstra said he did not think there was any sort of proclamation to businesses stating that they do not have to file.

Senator Townsend said that many corporations know that they have an obligation to file and are choosing not to. It is very different if they are hearing some sort of instructions from the State telling them they do not have to file if they have no unclaimed property, and that they would be doing the State a favor by not filing. He said that he would be shocked if that was the case but he wanted to get clarification from Secretaries Cook and Bullock that this was untrue.

Deputy Secretary Gregor stated that he wanted to be clear that these are property rights of owners. Those rights exist in perpetuity. The look-back period does not matter; it is always the owner's property.

Senator Townsend said that the unclaimed property framework is very mature. Delaware benefits uniquely from this situation despite the fact the goal is to reunite owners with their property. The cost and reality of doing business is that sometimes property is in a gray

area. The idea that the State would come in and take the property, and estimated property from years prior, is controversial. He found it interesting that the DOF's presentation did not mention estimation at all. His assumption is that contractors do estimate and that they do so at the instruction and guidance of the State.

Deputy Secretary Gregor said that was correct but the State approves the methodology the contractors use to estimate.

Representative Spiegelman said that the issue of the long look-back period is at the heart of the Temple Inland case in federal court.

Deputy Secretary Gregor said that if the State avoids property cases that are murky or that are in a gray area that would incentivize businesses to have sloppy record keeping as a way to avoid being audited.

Senator Townsend agreed but said that he found DOF's position that their focus was on returning abandoned property to the owner difficult to believe because the majority of the property ends up going to the State because it is owner unknown.

Deputy Secretary Gregor said that if a property is owner unknown it should not unjustly enrich the holder, it should be used for the public good.

Mr. Houghton said that it is much easier for businesses to pursue a claim if it is addressed property, but this is not often the case. The reason he is focused on the look-back period is because he believes that it is part of the system that needs to be modified.

Mr. Togman said that he agreed with Mr. Houghton. He asked Deputy Secretary Gregor how many companies filed in 1981.

Deputy Secretary Gregor said that he did not know.

Mr. Togman said that he has been in this field a long time. In 1981, the only people who were filing were banks and insurance companies because they were the only ones who knew about abandoned property and escheat. This is an issue of fairness. The point is that no one knew about this field in 1981 or 1986 and it is unfair to punish businesses today when they did not know they had to file back then.

Mr. Togman also stated that there is a real risk of federal legislation from these unfair practices. Since Delaware is an outlier among other states regarding the look-back period, the State should consider reducing the look-back period.

Representative Spiegelman agreed with Mr. Togman and Mr. Houghton, stating that the State is currently being sued on those grounds in the Temple Inland case.

Deputy Secretary Gregor said that he did not disagree that the look-back period as a matter of policy is something that may need to be reconsidered. However, he wanted to make sure that it was that aspect of the process that was being considered "aggressive" and not the behavior of the contractors. The policies of the department are separate from the behavior of auditors. He is willing to discuss changes in department policy that may make the department seem less aggressive.

Mr. Tuinstra asked if there are unclaimed property guidelines or best practices manual that has been published. California has their tax audit manual published online, including timelines. Making these guidelines readily and publically available could increase fairness.

Deputy Secretary Gregor said that there are guidelines approved by DOF but they are not published for the public.

Senator Townsend said that this is a great idea in theory, but it is likely that companies are going to be upset with the situation regardless of whether the process and guidelines are made available to them. The situation is that companies are participating in an auditing process based on sampling and estimation and are often required to write the State a check at the end of the process. He appreciates Deputy Secretary Gregor making the distinction between companies being unhappy with policies and being unhappy with the behavior of contractors. He also commends Secretary Bullock and Secretary Cook and their staffs for being flexible and willing to work with holders to make the process more palatable. It seems absurd that companies are not signing up for the VDA program offered by DOS after all the outreach Secretary Bullock has done. Senator Townsend said companies are gambling on whether they will be audited and he wonders if this is a breach of their fiduciary duties.

Senator Townsend asked Deputy Secretary Gregor if he had been speaking hypothetically when he said that the reason DOF has such long contracts with contractors is so there is a lower risk of them leaving in the middle of an audit and keeping the files and records related to the audit. That would violate Article V of the contract with Kelmar. He asked whether such a thing has ever actually happened. He asked if there was some way to negotiate that regardless if a contracting firm leaves in the middle of an audit, the State gets to keep the records and files from that audit.

Deputy Secretary Gregor answered that regardless of whether the State can keep the records, they would have to hire a new contracting company which may not want to use the records from the previous company.

Ms. Cross said that there have been cases that have been reassigned to different contractors. Holders are resistant to this because they have already spent time and money with one contractor and do not want to have to start over with another. In one particular case when this happened, DOF settled very favorably to the holder because they could not reasonably expect them to start over with a new contractor after more than three years of working with another.

Senator Townsend said that it seems like contractors leaving in the middle of an audit may be an eventuality. He said that the public has a right to be skeptical of using that as an explanation for why the State has such lengthy contracts with contractors.

Mr. Togman said that easy way to handle this would be to not assign any new cases to a contractor who leaves in the middle of a case.

Deputy Secretary Gregor agreed with Mr. Togman. If there is any sort of inappropriate behavior DOF would no longer assign that contractor cases.

Mr. Ratledge asked how many total audits were closed in FY 2014.

Deputy Secretary Gregor said they closed a tremendous amount in FY 2013, approximately 80 cases. In FY 2014 they closed 15- 20. It varies from year to year.

Thomas Collins, Delaware Bankers Association

(DBA), asked Secretary Bullock if he has spoken with companies that have chosen not to join the VDA program and if there is a particular reason they have not joined.

Secretary Bullock said he has not, since by definition these companies do not want DOS and DOF to know that they have not filed. He has heard some reasons secondhand, however. Some companies are worried about what their liability would be. He thinks the biggest reason that companies do not join is because they are not sure they will ever be audited. Large companies sometimes prefer to take the risk of being audited, which is 10% – 20%, than file.

Mr. Togman said that one consideration that was brought up by a company that presented to the 2006 Task Force was that the estimated cost for a client to be reviewed for their exposure for an audit is approximately \$2 million. It is not cost free.

Mr. Houghton asked if there is a connection between companies' decision to file or join the VDA program and DOF's decision to audit.

Secretary Cook said that those companies that have received letters to join the VDA but have refused are the focus of DOF for auditing. He said he has never, and has never directed his employees, to tell companies not to file.

Mr. Rosen clarified his earlier statement that he was not accusing anyone of telling companies not to file. However, because there has been no punishment previously for not filing it was a nonverbal message being perpetrated that it was okay for companies not to file. This ambiguity may be a reason to consider a shorter look-back period. It should be easier for companies to file and be certain of the statute of limitations and how long they need to keep their records.

Senator Lavelle said that the length of the contracts the State has with contractors is an issue worth examining further, since it is likely one of the longest contracts the State has with contractors of any sort. Shorter contracts could be rolled over if necessary. Senator Lavelle said it is important to infuse competition into the field to get better services and lower prices. Reliance on large companies like Kelmar does not do that.

## PUBLIC COMMENT

Senator Townsend asked if any members of the public wanted to comment on the Task Force's discussion.

Bob Byrd, Byrd Group, LLC., confirmed that The Council on State Taxation (COST) will be giving a presentation to the Task Force at the next meeting.

## CONSIDERATION OF TASK FORCE MEETING MINUTES

Senator Townsend asked the Task Force members if they had any comments or proposed edits to the Minutes from the previous meeting.

Mr. Togman stated that he had no changes to propose and that he thought the Minutes were very well written.

Senator Townsend thanked his Legislative Assistant, Michelle Zdeb, and Kiki Evinger, Legislative Aide to Representative Bryon Short, for their work preparing the minutes and organizing the meeting. The Senator then requested a motion approve the Minutes.

Representative Spiegelman motioned to approve.

Mr. Rosen seconded the motion.

The Meeting Minutes were approved, with all members in favor.

Senator Townsend thanked the Task Force members for attending and for their comments. He then noted the next Task Force meeting will be held on Wednesday, September 10, 2014 from 3 p.m. – 5 p.m. at Buena Vista.

The meeting was adjourned at 3:22 p.m.

# Minutes of the Meeting of the Unclaimed Property Task Force of Wednesday, September 10, 2014

Buck Library, Buena Vista State Conference Center, 3:00p.m. – 5:00p.m.

## Meeting Attendance–Task Force Members Present:

Senator Bryan Townsend  
Senator Greg Lavelle  
Secretary Jeffrey Bullock  
Thomas Collins  
Edward Ratledge  
Stan Stevenson, Esq.  
Robert Tuinstra, Jr.

Representative Bryon Short  
Representative Jeff Spiegelman  
Secretary Thomas Cook  
Michael Houghton  
Jordon Rosen  
Leonard Togman

## Absent:

Controller General Michael Morton

Representative of the Office of the Governor  
(Not yet appointed)

## Staff:

Michelle Zdeb

Kathryn “Kiki” Evinger

## Attendees:

Jamie Johnstone, DOF  
Michelle Whitaker, DOF  
Courtney Stewart, CGO  
James Hartley, Verus Financial  
Sara Lima, UPPO  
Doug Lindholm, COST  
Mark McQuillen, Kelmar  
Deb Zumoff, Keane  
James Dechene, DSCC

David Gregor, DOF  
Caroline Cross, DOJ representing DOF  
Bob Byrd, Byrd Group, LLC.  
Charles Hellman, Verus Financial  
Ferdinand Hogroian, COST  
Alison Iavana, DOS  
David Kennedy, Kelmar  
Freda Pepper, Keane

The Task Force Meeting was brought to order at 3:04 p.m.

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## CONSIDERATION OF MEETING MINUTES

Senator Bryan Townsend, co-chair, thanked the members of the Task Force and the public for attending the meeting. He addressed the first item on the Agenda, Consideration of the Meeting Minutes from August 12th.

Michelle Zdeb, Legislative Assistant to Senator Townsend, read in a memo describing the proposed changes recommended by Mr. Tuinstra. The recommendation made by Mr. Tuinstra Jr. related to making a name change on the last paragraph of page 7, where it stated his name instead of Mr. Rosen.

Senator Townsend asked if there were any objections to the changes. There were none.

Robert Tuinstra, Jr., Delaware Business Roundtable (DBR), motioned to approve the Minutes.

Representative Jeff Spiegelman seconded the motion.

The Meeting Minutes of August 12, 2014 were approved, with all members in favor.

## PRESENTATION BY COUNCIL ON STATE TAXATION (COST)

Bob Byrd, Byrd Group, LLC., said that he has represented COST for several years. COST is made up of approximately 600 member companies. COST has significant experience in the area of unclaimed property. The presenters are speaking on behalf of many national companies that have an interest in how Delaware handles this issue. COST and Mr. Byrd spent the last six weeks trying to convince representatives from member companies to attend the meeting and present, but they were unsuccessful. Mr. Byrd believes this is indicative of the tensions between businesses and the State. He then introduced the presenters from COST.

Doug Lindholm, President & Executive Director of COST, thanked the Task Force for inviting COST to present. COST became involved in the unclaimed property field in 2002. Delaware has historically been a great friend to Corporate America due to its business-friendly laws. COST is a strong supporter of unclaimed property laws and of consumer protection laws. There

are some aspects of unclaimed property, such as life insurance proceeds and payroll checks, which all parties agree should be returned to the rightful owner. He plans to focus on the “gray areas” of unclaimed property, mainly business-to-business transactions, in this presentation.

Mr. Lindholm began the presentation, titled ‘Corporate Experiences with the Delaware Unclaimed Property Program,’ by stating that many of the members of COST describe the Delaware Unclaimed Property Program as “frustrating.” Delaware holds a unique position as a state of domicile for Corporate America, but there are some aspects of the program that “frustrate” holders. Audits by contingent-fee auditors have been described by some holders as “aggressive.” Mr. Lindholm understands that the auditors are working within the statutory framework allowed by the law, but believes that the law allows for an unreasonable statute of limitations and does not have workable definitions of “unclaimed property.” The estimation techniques used by auditors create fictional unclaimed property and owners. Businesses do not need the “protection” of unclaimed property statutes.

Mr. Lindholm would like to see Delaware recognize that business-to-business transactions should not be subject to escheat. Credits in vendor accounts could arise for many reasons, including a duplicate check or an early payment discount. Estimation performed on those credit balances of all of the subsidiaries in a company often results in a multi-million dollar assessment. He does not believe there is any pretense of the property being returned to the rightful owner. The market does a good job of removing poorly performing companies. If a company has a significant amount of debt, then perhaps they should not be in business in the first place.

In 2012, the Department of Finance (DOF) put the 1981 look-back in writing for the first time and temporarily limited the look-back to 1986 (16 DE Reg. 530). Businesses need certainty in statutes. The fact that it took so long for this to be officially written in the statute does not provide that certainty. This lengthy look-back is also not in line with what other states are doing. The Uniform Unclaimed Property Act (1995) recommends a ten-year statute of limitations. The American Bar Association (ABA) recommended a three-year statute of limitations to the Uniform Law Commission. Standard corporate recordkeeping

practices for businesses require keeping seven years of records. Delaware's statute of limitations is far longer, requiring businesses to keep 28 years of records.

Approximately 15 states employ a business-to-business property exemption, which ABA and Unclaimed Property Professionals Organization (UPPO) have endorsed in filings with ULC. Several other states are considering legislation which would allow this exemption. Businesses are in the best position to enforce their rights. Additionally, 44 states have adopted some version of the ULC Model Uniform Unclaimed Property Act (UUPA), which provides uniformity, definitions and best practices. Delaware has not adopted a version.

Mr. Lindholm introduced his colleague, Ferdinand Hogroian, to continue the presentation.

Ferdinand Hogroian, Tax & Legislative Counsel at COST, said that one of the main concerns that companies have is estimation. The majority of the companies that make up the COST Unclaimed Property Task Force have filed every year and they are still audited and subjected to estimation. Delaware first enacted the statutory authority for estimation in 2010. The *Select Medical Corporation v. Cook* (2014) and *Temple-Inland Inc. v. Cook et al* (2014) cases in federal court both focus on whether Delaware can retroactively apply estimation and whether estimation actually results in an appropriate approximation of escheatable property.

Mr. Hogroian said the concerns expressed in the *Select Medical* case mirror the concerns COST companies have about the Delaware Unclaimed Property Program.

Senator Townsend asked for clarification about where the quotes Mr. Hogroian was using in his PowerPoint presentation came from, specifically whether they were from the plaintiff's complaint or were a judicial finding.

Mr. Hogroian said that the quotes he was using in the presentation were from the complaint in the case. However, these sentiments were not limited to the complaint in the case; the concerns are echoed by COST member companies.

The estimation includes property escheatable

to another state. The estimation methodology takes errors from the current period where there are records and extrapolates that error rate to other periods. Even though this is not Delaware property, it is considered escheatable to Delaware. The property may be escheatable to another state but not remittable, such as if the state has a business-to-business exemption. There is property included in the assessments that appears to have been returned to owners before it became dormant. Sometimes a check has been canceled and then reissued. This is not unclaimed property yet is being included in the estimation in error. Additionally, the use of estimation methodology for one year applied to entire periods makes the assumption that there is a constant level of unclaimed property from year to year even when the data does not support that. In that circumstance, the estimation methodology is suspect. This process of estimation creates property to be escheated to Delaware that is not necessarily Delaware property.

Mr. Hogroian presented a list of recommendations to reform the escheat process. He said that estimation should never be used when a holder's records are substantially complete. Estimation should be based on property reportable to Delaware and not to another state, regardless of whether that state requires escheat of the property. The statutes should describe all property that is subject to escheat; if the holder is not on notice then they cannot report the property. COST also recommends applying a reasonable statute of limitations period for current and future audits that is more consistent with reasonable recordkeeping requirements. The statute of limitations should run from the time a report is filed in good faith and should apply to all property. In order to reform the audit process, Mr. Hogroian recommended specifying standards for audits, adopting transparency measures, enacting penalty reform, and ending contingent fees.

Mr. Lindholm concluded COST's presentation by reminding the Task Force that Delaware is the domicile of many companies. The United States Supreme Court's (SCOTUS) ruling that unclaimed property without any address is escheatable to the state of domicile is extremely beneficial to Delaware. However, this ruling – when combined with the contingency fee auditors receive (causing them to maximize amounts), estimation, and the long look-back period – makes this business climate unpalatable for Corporate America. The fact that penalties are used as a negotiating tool by the State

and that there is no independent tribunal for review of cases does not make the business climate welcoming. Other states sense this and would likely be pleased to have some of the businesses currently incorporated in Delaware incorporate in their state. Other states are modifying their corporate and unclaimed property statutes in order to compete for these businesses. Mr. Lindholm hopes to work with Delaware officials to amend statutes to ensure a friendlier environment for Corporate America in Delaware.

Representative Spiegelman asked if a list of suggested changes to the Delaware statute, submitted by all groups that have presented to the Task Force, would be compiled so that he would know what possible recommendations could be made to the General Assembly.

Senator Townsend said that could be done.

#### PRESENTATION BY VERUS FINANCIAL

James Hartley, Esq, CEO of Verus Financial, stated that Verus is an unclaimed property auditing firm that conducts unclaimed property audits on behalf, and at the direction, of Delaware and Verus' other 45 client-states. Verus was founded on the principle of addressing the issue that life insurance policy holders across the country were dying with no beneficiaries named and the funds, after a dormancy period, were being declared as unclaimed property. These audits have had a profound impact on the life insurance industry and on countless lives. It is because of states like Delaware who support Verus that they are able to do this work.

Verus has reached a resolution in approximately 70% of life insurance cases. It is a complex process. Verus conducts complex multi-state audits, requiring a high degree of specialization as well as the use of sophisticated computing and data processing algorithms and systems. It would not be practicable for Delaware to conduct these audits on its own without the assistance of third-party auditors, such as Verus. By performing these audits on a multi-state basis, Verus makes it possible for Delaware to ensure compliance with its unclaimed property laws in an efficient manner that minimizes the burden on the companies being examined.

Mr. Hartley explained the process of investigating an unclaimed life insurance policy payment. Verus meets with life insurance companies and enters into

non-disclosure agreements with them. Verus asks the companies to provide them with their policies and procedures so that they know if the company has procedures in place to allow them to identify property that should be reported to the State. While analyzing data that they have received from the company, which is a long and involved process, Verus engages in dialogue with the company to agree upon an audit template. This increases transparency and can provide for a mediation solution in case of conflict, although Mr. Hartley noted that there has only ever been one dispute and it was satisfactorily resolved. Verus has this type of agreement with 17 major life insurance companies.

As a result, Verus has uncovered about \$2 million in unclaimed death benefits across the country. Verus works with the company to verify that the names they uncover match their records (name commonality is an issue) and what, if any, benefits are owed. Following the identification of unclaimed property during the audit, Verus works with the holder to reconcile any issues the holder may have with items contained on the report. After it is agreed that unclaimed property identified during the audit is subject to remittance, Verus works with the holder to ensure that appropriate due diligence is performed to try and locate and pay the owner prior to the property being reported to the State. As part of the examination process, Verus informs the holder of their continuing statutory obligation to report unclaimed property of the type identified during the examination and to follow any required due diligence when reporting that property in order to ensure compliance going forward and minimize the need for future audits. Companies are usually pleased with the service that companies like Verus supply because they do not have the technology to keep up with unclaimed policies, since some beneficiaries do not know that the policyholders had a life insurance policy and do not file to claim it.

Mr. Hartley discussed Verus' compensation. Verus is compensated on a contingency-fee basis only for unclaimed property that is actually delivered to its client-states after reconciliation with the holder and due diligence is performed to try and locate and pay the owner. Verus is not compensated at all for unclaimed property that it identifies during the audit if the owner is able to be located and paid before the property is delivered to the State. In audits Verus has conducted, a significant amount of the unclaimed property that it has

identified has been able to be reunited with the owner through the due diligence process.

Charles Hellman, Esq., Vice President & Managing Director of Verus Financial, stated that the results of Verus' audits provide concrete benefits to Delaware citizens by reuniting them with their property. He then gave examples of two audits where death benefits were paid directly to Delaware beneficiaries. Verus did not receive any compensation for these audits, since the beneficiaries were found before the money went to the State.

Mr. Hellman showed a video that was produced for other state-clients and that showed clips of interviews of beneficiaries who had received a life insurance policy payment due to Verus' investigation into the unclaimed benefit. Mr. Hellman stated that there were thousands more stories like the ones in the video. Having a longer look-back period is helpful because it allows Verus to reunite more owners with their property.

Mr. Hartley stated that the average payment on a policy is \$2,000 and the policyholder on average has been deceased for thirteen years.

Senator Greg Lavelle said that he is glad that the insurance companies are increasing their due diligence. He asked about how many policies Verus reconnects with beneficiaries.

Mr. Hartley said that it depends on the type of the policy. If the policy is one of the older ones that used to be sold door-to-door then it is unlikely that they will be able to find beneficiaries due to poor recordkeeping. On other policies he estimates that there is a 30-40% success rate reuniting beneficiaries with payments.

Senator Lavelle asked if Mr. Hartley knew how much property had been reunited with Delawareans.

Mr. Hartley said that there have been 2,600 policy holders with \$4.7 million in unclaimed property sent to DOF.

Senator Lavelle said that this seems like a perverse incentive, since Verus gets paid only when money is escheated to the State.

Mr. Hartley said that there are due diligence process

steps that must be followed before the property can be escheated to the State. There are a variety of methods which the holder can use to try to find the beneficiary. There is legislation pending in many states that requires life insurance companies to check the Death Master File (DMF) to see if the insured is deceased.

Senator Lavelle asked how much the State of Delaware has paid Verus in the past couple of years.

Mr. Hartley said that they received about 10.5% of the \$4.7 million that was escheated to the State.

Stan Stevenson, Esq, Delaware State Bar Association (DSBA), asked if Verus only audits the insurance industry. He also asked if Verus only audits payments of policy benefits or if they audit other aspects of the companies as well. Additionally, does Verus use estimation?

Mr. Hartley said that Verus has only audited the insurance industry in Delaware. Verus does not use estimation.

Robert Tuinstra, Jr., Delaware Business Roundtable (DBR), asked if Verus requests a significant amount of information from insurance companies or if it would be a simple request to accommodate.

Mr. Hartley said that Verus specifically requests the company's life insurance data. That data is then normalized and analyzed by Verus. It's an involved process.

Mr. Tuinstra clarified that Verus is asking companies for its list of people insured.

Mr. Hartley said that is correct. Non-disclosure agreements prevent Verus from using that information for any other purpose.

Mr. Hellman said that Verus looks at death benefits as well as matured annuities and retained benefit asset accounts. They look at policyholders who are alive as well. There is also a settlement option.

Mr. Stevenson asked if Verus audits companies for their business-line profits as well.

Mr. Hellman said yes.

Mr. Tuinstra asked if the majority of Verus audits were of owner-known property.

Mr. Hartley said yes. If the beneficiary's address is unknown, it is presumed that it is the same as the insured. It is very rare to have owner-unknown property.

#### PRESENTATION BY KELMAR

Mark McQuillen, JD, President of Kelmar, thanked the Task Force for inviting him to present. He hopes that his presentation will provide some clarity into what Kelmar does and will help the members when they formulate their final report.

Mr. McQuillen described the unclaimed property case of *Texas v. New Jersey* (1965). This was a case that involved the issue of jurisdictional priority that was disputed by four states. Sun Oil Company drilled for oil in Texas, was incorporated in New Jersey, had headquarters in Pennsylvania, and had a last known address in Florida. This is a debt that is owed, not an asset of a holder. When deciding this case where jurisdictional priority is in question, the court considered: which state was in the best position to return the money to the rightful owner, how to minimize conflict between the states, the ease of administration and clarity, and how to avoid unjust enrichment of the holder. This court case recognized that all of the states had a claim to the priority, but that some claims were stronger than others. They ranked the claims from strongest to weakest as follows: name and address on books and records of the holder, the state of incorporation, state of allocation, and then the state with any nexus.

The nature of businesses is that small businesses send goods and services up to big businesses while big businesses send money down to small businesses. Abandoned property is big businesses sending the property to the small businesses. According to the Small Business Association (SBA), 80% of businesses are sole proprietorships, 98% have fewer than twenty employees, 99.7% are considered small businesses by SBA, and on average small businesses employ 1.95 people. A business-to-business exemption would affect all businesses, not just the larger ones. Small businesses do buy from big businesses, but these are not part of a bilateral economic relationship. These sales are done on the retail side of big businesses where there is a disproportionate economic relationship.

Mr. McQuillen said that there are many reasons to have a business-to-business exemption. Small businesses do not have many employees; they cannot afford the "red tape" of compliance. Small businesses are almost always the creditor, not the debtor. Bigger companies do not need statutory help to protect themselves against other businesses. Businesses also do not operate bilaterally; it is a multilateral system. Business-to-business exemptions can end up hurting companies in the state. For example, Ohio (OH) has a business-to-business exemption. If an OH Company owes the State of California money, they are required to pay that debt. However, if a New York (NY) company owes an OH company, the NY company is not required to pay the State of OH for the debt it owes the OH company because OH has a business-to-business exemption. OH businesses then lose out on monies owed. Business-to-business exemptions actually hurt in-state citizens and help out-of-state companies.

Exempting unclaimed property does not violate federal due process. An exemption is not converting the debt of a holder into the asset of a holder. Rather, it is simply stating that the State Escheator will not become the custodian of the property for consumer protection purposes. Holders often presume that an exemption enacted by the state legislature is a lawful conversion of a holder's debt to a holder's asset, but it is not. The holders cannot "keep" the funds. The state legislature can choose to not pursue finding the rightful owner but it is unconstitutional to allow that property that is owed to someone else be kept by the holder.

Senator Townsend asked if Mr. McQuillen thought it would be beyond the power of the State to regulate the definition of unclaimed property.

Mr. McQuillen said yes. He believes that a debt on the books of a company is a debt. There is a distinction between what is a debt and if the State is willing to step in to enforce that debt being repaid. Whether or not that debt is defined as unclaimed property is a different issue, for example a \$5 gift card would not be considered unclaimed property. The holder should not keep the property.

If the state of address does not want the money or does not have supporting documentation to show that it should be sent to them, then estimation is often used.

Mr. Tuinstra said that he agreed with Mr. McQuillen's statement that if a debt is on the books of a company it should be paid. He asked how that logic fit with estimation.

Mr. McQuillen said that estimation is used when books and records do not exist. Estimation and projection are used by Kelmar and most other public accounting firms. It is just math. The state legislature has to decide what the appropriate amount of time to look at is for estimation; the period of estimation varies between states.

Mr. Tuinstra asked if Mr. McQuillen would agree that the result of estimation is that it creates property which can never be reunited with a real owner.

Mr. McQuillen said that was true. Unless records show up later, estimation produces a product that can never be returned. However, if the property is in the holder's bank account it can also never be returned. Most of the money Delaware receives has names and addresses on it; only 8% is received as a result of estimation.

Mr. Tuinstra asked if the 8% Mr. McQuillen mentioned referred to Kelmar or all of the revenue the State of Delaware receives in unclaimed property.

Mr. McQuillen said that it referred to the State of Delaware.

Mr. Tuinstra asked if that meant that 92% of the property Delaware receives is owner known and has an address.

Mr. McQuillen said yes. Some of that property is foreign, and approximately \$600-700 million in foreign property was returned last year. Billions of dollars are returned nationwide before the company is audited because the owner is known. Billions of dollars are returned prior to assessment.

Deputy Secretary David Gregor, Department of Finance (DOF), said that property with a foreign address is returned.

Senator Townsend asked Mr. McQuillen to clarify what he meant when he said that 'billions of dollars are returned prior to assessment.' He asked if the property

was returned as a result of the current system being in place and functioning correctly.

Mr. McQuillen agreed with Senator Townsend and said that was what he meant.

Michael Houghton, Esq., Uniform Law Commission, said that the Task Force understands that businesses are upset to find that if they are incorporated in Delaware, but have no other form of operations in the State, that Delaware has a claim on their unclaimed property. He also understands that businesses are suspect of the auditing firms, like Kelmar, because they get paid such large contingency fees.

Mr. McQuillen said that he understands the concerns that Mr. Houghton described, but said that it is important to question whether it is better to have this sort of system or to let the funds enrich the holder. Mr. McQuillen presented at a previous Unclaimed Property Task Force (2006) in Delaware when similar concerns were raised about the auditing process. The Task Force then feared that the auditing process would cause companies to become incorporated in other states, leading to a loss of revenue for Delaware. This has not happened, and Mr. McQuillen does not think it will. The benefits that companies receive by being incorporated in Delaware vastly outweigh any hardships caused by the auditing program.

Senator Lavelle suggested making the escheat environment more competitive so that the State does not have to pay auditors so much.

Mr. McQuillen agreed that increasing competition would be one way to make the unclaimed property business less lucrative for his company. However, he said that Kelmar is currently unmatched by other companies in terms of the resources, expertise, and services they can provide.

Edward Ratledge, public, University of Delaware Director of the Center for Applied Demography & Survey Research (CADSR), requested that some information about the sampling techniques these companies use and their accuracy be presented to the Task Force.

Senator Townsend said that topic would be discussed later in the meeting.

## PRESENTATION BY UNCLAIMED PROPERTY PROFESSIONALS ORGANIZATION (UPPO)

Sara Lima, Esq., of Reed Smith, representing UPPO, said that UPPO is a non-profit trade organization similar to COST. They have hundreds of member companies. UPPO members identified some concerns that would be of interest to this Task Force.

Ms. Lima referred to the handout provided by UPPO titled “Unclaimed Property Professionals Organization Requests for Task Force” and to the letter dated September 8, 2014 that Toni J. Nuernberg, Executive Director of UPPO, wrote to the Task Force. One of the biggest requests that the holder community has is to define and clarify what constitutes owner “contact” sufficient to toll the dormancy period. This is especially difficult when it comes to dealing with long-term investment property. When a company escheats shares of stocks to the State of Delaware, the State is entitled to sell those shares and does not have a waiting period for selling them. If an owner is later found for the shares, they receive the value of the shares from when the State sold them. This is frustrating because the value of the shares may have increased (or decreased) by that time, and frustrated owners may bring litigation against the holder. UPPO recommends limiting the post-escheat sale of securities in order to protect shareholders from loss and holders from litigation.

Ms. Lima stated that UPPO does not believe that estimation should be eliminated completely. However, UPPO does recommend limiting estimation to “reasonable” methods and that it should be used only as a penalty when holders have failed to meet defined record retention requirements. There are some ambiguities in the audit process that have caused disputes. There is also a perception that because auditors are paid a contingency fee, that they inflate the amount of property that is required to be escheated to the State. Therefore, UPPO recommends increasing guidance to contract auditors and/or revising the incentive provisions to reduce any perception of impropriety.

Additionally, UPPO recommends refining Delaware’s administrative process to be more impartial and to allow holders the opportunity to interface with representatives of the State during an audit. UPPO would like a written acknowledgement that holders have the right to communicate directly with the State

if there is a dispute. The holders would also like to have some say in who arbitrates disputes in order to make the process more impartial.

Deputy Secretary Gregor said that with respect to the sale of securities, there was an examination of the securities industry. It was discovered that due diligence was not being done to the extent DOF thought. Since it was found that due diligence was not being done appropriately by holders, now when the State receives escheated shares they do another round of due diligence before selling the shares. Last year DOF returned approximately \$60 million in securities. Due diligence for securities might have been a problem before but Deputy Secretary Gregor does not believe that it is anymore. DOF also states in its engagement letter that they welcome the opportunity to interface with holders. However, advocates for holders often advise against this.

Michelle Whitaker, DOF Audit Manager, said that she communicates in writing and verbally that she is the final arbitrator in any dispute. DOF is doing everything possible to communicate with holders and to make the audit process clear.

## OPEN DISCUSSION BY TASK FORCE

Mr. Ratledge said that he has done a lot of work with complex sampling design and believes that almost anything can be measured. He asked what the sampling method was that Kelmar used in audits and if they checked their accuracy in estimation against the records of the company.

Mr. McQuillen said that they do check their accuracy. In one case they used estimation and then additional records became available going back to 1971. Kelmar’s estimation mirrored those records and was well within the margin of error. Kelmar’s statisticians seek to have a 90% confidence rate. Many states use the same estimation/projection calculations as Delaware and have similar results. He said the Task Force should focus on what the role of estimation should be rather than the math of the equations used to estimate.

Mr. Ratledge asked if someone monitors the quality of the sampling.

Mr. McQuillen said yes. The state-client vets the process as well. In terms of Delaware, Kelmar auditors

meet with Delaware DOF members, such as Michelle Whitaker, every month and go over every single audit that is in process and DOF makes all of the decisions. The contingency fee Kelmar receives is decided by the State.

Secretary Thomas Cook, DOF, wanted to clarify that the estimation process is not conducted solely by the State. The holder is also involved in the decision-making process of the methodology and estimation.

Mr. McQuillen said he agreed with Secretary Cook. He said that there is a healthy tension between the State, the holder, and the advocate about what records should be included.

Ms. Whitaker confirmed that the State is in contact with both the auditors and the holders. If a holder believes that a decision is not fair and can provide support that it is unfair, Ms. Whitaker is open to reconsidering a decision.

Mr. Stevenson said he was surprised to learn that estimation is only used in 8% of unclaimed property cases; he had thought that percentage would have been much larger.

Senator Townsend asked if any state official disputed that estimation is only used in approximately 8% of unclaimed property cases.

Deputy Secretary Gregor said that 8% is probably an accurate number, but that they would want to check in order to be certain.

Mr. Houghton said that he would like to see a historical view of that number, such as what the rate was over the past ten years.

Senator Townsend said that he and Representative Bryon Short would be in touch with DOF before the next Task Force meeting in order to make sure that the Task Force is supplied with the data they have requested.

Mr. Tuinstra said that if estimation is used in such a small percentage of unclaimed property cases, then the impact of eliminating estimation would seem to be minimal. He asked if this was correct. He then asked what percentage of Kelmar's audits utilize estimation.

Senator Townsend said the first question Mr. Tuinstra asked would be a matter of policy.

Mr. McQuillen said that in terms of the audits that Kelmar does for Delaware, approximately 50% of the audits use estimation. There are a lot of subcategories that may or may not use estimation.

Jordon Rosen, Delaware State Chamber of Commerce (DSCC), asked if 50% of the audits for Delaware involve estimation. He had heard earlier in the meeting that the total revenue received from using estimation was only 8%.

Deputy Secretary Gregor said that the 8% refers to all the revenue that is collected, whether it is through a VDA or annual filing. The 50% refers to the estimations Kelmar does.

Senator Townsend asked for clarification. He asked if the 50% meant that half of all audits involve estimation, or that half of all revenues collected come via estimation.

Mr. McQuillen said that in an examination there are two services that Kelmar provides. One service is in securities. Most of that area has names and addresses, so virtually none of those audits would use estimation. In contrast, general ledger audits almost always involve projection and estimation. Whether or not estimation is used depends on the type of audit being done, the nature of the business involved, and what sorts of records are available. If Delaware decided to completely eliminate estimation, half of the audits Kelmar does would go away. A lot of Delaware's annual filings would also go away because audits play an important role in ensuring compliance.

Senator Townsend asked if Mr. McQuillen was saying that the estimation part of that 50% constitutes less than 10% of all revenues from Delaware's unclaimed property program.

Mr. McQuillen said yes.

Deputy Secretary Gregor said that it is important to understand that if estimation is not available as an alternative, DOF will not receive the records they need to do an examination. The 10% is not a static number.

Senator Townsend said he looks forward to seeing concrete data from DOF to support the figures that were being discussed. Given the complaints that the Task Force has heard about the lengthy time period that companies are required to keep books and records, he asked how often estimation is used to audit companies that have chosen never to file.

Ms. Whitaker said that when an examination is being done, the company's filing history is taken into account. Companies may be upset about estimation, but if they would maintain their records it would not have to be utilized.

Senator Townsend asked if companies are being told to keep records for 15-20 years, or if they chose not to file then the consequence is estimation will be used. He asked if anyone had a problem with the latter.

Mr. Stevenson said that is what companies are told. The way the statute currently reads is companies only have to file if they have property to report. A company that is incorporated in Delaware but that operates entirely in California would never have any occasion to file a Delaware unclaimed property return because they would never owe anything to Delaware.

Ms. Whitaker corrected Mr. Stevenson's statement by stating that the company would have to report if it had any unknown items.

Mr. Stevenson agreed with Ms. Whitaker. If the company gets audited thirty years later, they would be unable to defend themselves against estimation even though they were not required to file in Delaware.

Senator Townsend asked how many of those types of companies are the ones expressing concern and are subject to being audited.

Ms. Whitaker said that if a holder can produce their filing history to DOF, those years are not subject to estimation. They get credit for filing.

Mr. Houghton said that would assume that the holder has kept their filing history for 30 years. Many companies believe that is too much, particularly since the State of Delaware would not be able to produce their records from thirty years ago.

Senator Townsend said that was extremely ironic.

Mr. Tuinstra asked what level of records auditors would be looking for and for what period of time.

Mr. McQuillen said they would usually ask for 3-4 years of records or whatever is agreed upon with the holder within the statute of limitations.

Mr. Tuinstra asked if on average the auditors would be looking to find transactional-level records and how far back they would be looking for those records to be kept.

Mr. McQuillen said that they would be looking for transactional level data. North Carolina requires that level of records be kept for fifteen years. Kelmar used to ask for at least five years of records, but they received complaints that the auditors were not really trying to reunite property, that they were just looking for an excuse to use estimation. Then they started asking for all records going back to when the company was started and they were called "aggressive." Now, Kelmar asks for as many records as the company has and goes from there. There is no definitiveness and the process depends on many factors, such as the size of the company and mergers/acquisitions. Most records they receive are electronic. Kelmar takes direction from their client-states on how many years of records to ask for.

Mr. Rosen asked if there were any restrictions on what documents an outside contractor can request from the holder.

Ms. Whitaker said no. The statute allows for all records to be requested.

Mr. McQuillen said that Kelmar signs confidentiality agreements with all holders to ensure confidentiality of any records they receive.

Ms. Whitaker said she knew of one case when a holder reported an unknown item through the VDA program. Within a year and a half, the claimant came forward with documentation that was provided to them by the holder that substantiated the claim that that particular item should have never been reported to Delaware. The State of Delaware is very concerned about making sure that no property comes to Delaware that it is not entitled to.

Secretary Cook asked the representatives from COST if they agreed that if there is no filing history that DOF should be using estimation.

Mr. Lindholm said that he wanted to point out that not all companies are obligated to file. He hears information from companies that have gone through audits. In terms of Mr. McQuillen referring to unclaimed property as a "debt," Mr. Lindholm said that it may not be a debt but may be a credit balance or bookkeeping error. The basis of estimation is larger than unclaimed property. Holders are not unjustly enriched by keeping unclaimed property.

Senator Townsend referenced the language from the Select Medical complaint COST used in their presentation. He said it is not a judicial finding, but an opinion from the claimant. He asked if Mr. Lindholm was saying that Kelmar and other auditing companies are not making adjustments for those situations. He wants to make sure everyone's intentions are clear and that the Task Force is discussing what is actually in the system.

Mr. Lindholm said that in the complaint in Select Medical, they were willing to argue everything mentioned. The case was settled by the State of Delaware for \$0; they were not assessed anything at all. He recommends taking a look at that complaint. He does not believe that case involved unclaimed property at all.

Secretary Cook said that in the Select Medical case, the State of Delaware asked for records numerous times and was denied. The assessment of \$0 was made once the State was given access to the company's records.

Mr. Lindholm said he did not know the specifics of the case, but it seemed to include items that were not unclaimed property being included in estimation.

Secretary Cook said that the point was that companies are not filing and not submitting records to the State. The VDA program that was created by Secretary of State Jeffrey Bullock and the outreach that department does specifically targets companies that have never filed.

Mr. Hogroian said that many of the member companies that COST works with are not eligible for the VDA program.

Secretary Cook said that those audits must have been started prior to the last two years. That is where the audits are coming from

Mr. Hogroian said that there are some ongoing audits and some have settled recently. Their complaints about the audit process and estimation are current.

Senator Townsend said that was a fair point to note, but that it was also important to acknowledge the changes that have been made in the last couple of years to improve the audit process. He then asked if estimation was being used to "explode" the error rate in company's filings or the underreporting rate in order to justify overcoming the statute of limitations.

Mr. McQuillen said that he only does the math. Other people determine whether or not the error rate "explodes." He said that he does his job extremely well and does not think that he makes any judgment calls that benefit his company. He does not believe that is happening at all.

Mr. Hogroian said that according to the numbers he has, property that has an address outside of Delaware is extrapolated backwards and then taken as Delaware property. If the holder keeps the property, it can still be claimed by the owner at a later date. It does not have to be given to the State of Delaware. He does not think it is right that property with an address in another state be given to the state of incorporation.

Mr. Houghton said that what is right or wrong can be argued about this issue, but he believed Kelmar would say that incidents of unreported property (even if it is owed to another state on an address basis) constitutes a more recent experience of unclaimed property. When this is extrapolated backwards over time, this does create a number but it is one that cannot be directed to other states based on addresses. COST is saying that the only type of extrapolation that should be done is take a Delaware corporation, identify the items of unclaimed payroll and accounts payable/receivable in Delaware (which will be small) and then estimate back based on those figures. That is not the rule Kelmar uses. Many of other auditors use the same methods as Kelmar.

Senator Townsend asked if people were disputing the amount of unclaimed property or which state it was assigned.

Mr. Hogroian said that it depends on the statutes that other states have.

Mr. Houghton said that proving which state the property should go to is difficult if there are no records proving that it should go to one state over another.

Mr. Hogroian said regardless of whether the other state requires the escheatment or it is put outside the statute, it should not be reported to Delaware.

Mr. McQuillen said that SCOTUS decided that if the property is not claimed by the addressed state it goes to the state of incorporation. The holder should not keep it. The juxtaposition of COST's position is that they say that people have complied with filing and now their records are gone and they cannot prove their compliance, but there are also people who have not complied. Those people want the property to only go to one or two people in Delaware and have the majority of the property go to another state. The property would either go nowhere or go to another state.

Senator Townsend said that the issue of whether the money does not go anywhere or is sent to another state is important to discuss.

Ms. Whitaker said that anything that is estimated under their agreement they are indemnified for. If proof can be shown that the property belongs to another state, DOF will pay that claim to the claimant.

Mr. Houghton said that the problem was that there would be no claim because no records exist to prove the claim. However, he agreed with Mr. McQuillen that this was a SCOTUS decision. The Delaware legislature can decide the extent it is to be applied, but this was the decision reached by SCOTUS.

Mr. Lindholm agreed that the SCOTUS decision said that unknown property should go to the state of incorporation, however he questions how that property is identified. COST alleges that the audit process is very aggressive, factors in errors to other states, and assumes that the amount of unclaimed property will be the same from year to year.

Senator Townsend asked if COST is alleging that the statistical models that Kelmar and other auditing companies use do not allow for those variables. He asked

Mr. McQuillen if the models that Kelmar uses assume that there will be the same rate of unclaimed property every year or if they have found that Corporate America tends to have complied at different rates over different time periods. He asked to see concrete examples from Corporate America about what is going on.

Mr. Hogroian said that in the case of Select Medical, the matter was resolved by the courts and it was found that Delaware was not entitled to the property.

Mr. McQuillen said it was his opinion that neither his company nor the State is behaving aggressively in audits. The Task Force has heard a lot of anecdotes, but no one has come forward to testify or give specific examples of their experiences.

Ms. Lima said that in the letter from UPPO they do detail specific areas of dispute in the estimation process.

Mr. McQuillen said that is different than calling the auditing process "aggressive." The issues described in the UPPO letter are ones that there can be dialogue around and changes made.

Senator Townsend said that how "aggressive" behavior is defined is in the eye of the beholder.

Mr. Rosen said that he thinks that "fairness" should be substituted for "aggressiveness." That is really what the holder community is looking for. Corporate America likes certainty, and the statutes should be very clear about what is expected of them. This Task Force is supposed to ensure that the audit process is fair for both the State and the holder.

Senator Townsend reiterated that he would like examples of specific aspects of the audit process that are unfair identified. He would like examples of specific companies who have always filed but who have been subject to estimation techniques that have eliminated the statute of limitations.

Ms. Lima asked if Senator Townsend was referring to holders that have filed or ones that can prove they have filed.

Senator Townsend said he was referring to those that have filed.

Ms. Whitaker said that just because a holder has filed does not mean that they have filed accurately or reasonably.

Senator Townsend said that he understood that. However, the system is structured so that once a holder files the statute of limitations kicks in.

Mr. Rosen said that in tax the statute of limitations is three years. If the government does not audit by then, and there is no instance of fraud, then the statute of limitations has tolled and no further audits of that time period can be done. He does not think Corporate America feels the same way. If the State audits them twenty years later, they will most likely be vulnerable since they do not keep records that long.

Senator Townsend asked how many instances are there of companies that have filed being audited and subject to estimation because they no longer have their records, as opposed to companies that have never filed.

Mr. Tuinstra asked Mr. McQuillen what portion of the audits they perform for Delaware where they do a look-back to 1986 are of companies that have not filed versus those that have a substantial underpay.

Mr. McQuillen said that he is not directly involved in the auditing process so he can only speak anecdotally. He said that most of Corporate America does not file, or if they do they file very small amounts or very specific and discrete amounts. It is theoretically possible that a company could be in very good compliance and then not be able to prove that in an audit, but that is not the experience that Mr. McQuillen has had. In his experience, companies are either in no compliance or marginal compliance.

Mr. Tuinstra asked in the marginal compliance scenario how long of a period of time is there to audit.

Mr. McQuillen said that was a policy question he could not answer.

Senator Townsend said that the Delaware Code lays out the statute of limitations.

Mr. Tuinstra asked if in the audits that determine whether a company has underreported, conducted during the appropriate statute of limitations, if the look-

back period goes back to 1986.

Mr. McQuillen said that they accumulate the books and records for an initial review and then the audit team meets with Ms. Whitaker to determine what the records mean and their relevance. The determination about how far back the audit goes is determined by Ms. Whitaker on a case-by-case basis.

Mr. Tuinstra asked if that system applies to both filers and non-filers.

Mr. McQuillen said that it applied to both.

Mr. Houghton said that from 1981-2001 there was no statute of limitations in Delaware.

Secretary Cook said that he wanted to clarify what was said about the credits companies get for filing and being used for estimation. Those are only looked at as credits if they are taken as income.

Mr. McQuillen said that they look at credits that are currently on the books and records that have reached the dormancy period and have not been resolved. The vast majority of the items they examine have been taken off the books. Kelmar works very closely with the holder and the advocate to figure out which are accounting errors and which are not. It's a complicated process, but it has rules and if the company is not happy with the end result they can appeal to Ms. Whitaker.

Mr. Lindholm said that companies are in the position that they have to prove that the property is not unclaimed property, which is difficult to do since they may not keep records that extend that far back. There are many other reasons that a credit could appear in a company's accounts.

Senator Townsend asked if Mr. Lindholm was saying that auditing companies do not take those factors into account in their calculations.

Mr. Lindholm said that was correct. There is no way to verify accuracy with estimation.

Senator Townsend said that some of the comments made to the Task Force made it seem like the estimation calculations that companies like Kelmar are doing are very rudimentary and inaccurate. The concerns that are

being expressed are valid, but Senator Townsend wanted to make sure that the auditors are using advanced techniques to adjust for variables.

Mr. Lindholm said that he gets his information second-hand from COST's member clients. The concerns have also been expressed through litigation.

David Kennedy, JD, Kelmar General Counsel and Principal Member, said that Kelmar goes through the audit and the holder gets the opportunity to prove that the credit balance or duplicate entry was resolved in another way. Those adjustments are made in every audit. Those items that the holder cannot prove were resolved in another way have to be left in the audit. Holders who do not think that is appropriate seek mediation with Ms. Whitaker.

Senator Townsend said that he understands that there is a disagreement about whether that is fair. He wanted to know how many companies have been subjected to this process and have filed versus those who have not filed.

Mr. Lindholm said that companies would be much more comfortable being incorporated in Delaware and having their businesses in the state if the look-back period is significantly shortened.

Senator Lavelle suggested that if companies are afraid to testify to the Task Force about their experiences that perhaps they can speak in private and have that testimony shared. He asked if the contracts that Kelmar has with other states are similar to the one they have with Delaware, particularly the length of the contract and the contractual obligations. He also asked if Kelmar entered into simultaneous contracts with other states.

Mr. McQuillen said that Delaware does have one of the longest contracts with Kelmar compared to the contracts Kelmar has with other states. However, this time length is not unique when compared to the time length of contracts that the State of Delaware has with other auditors. Kelmar has represented other states as long as they have represented Delaware.

Senator Lavelle said that he does not know of many other vendors that the State would enter into such a long contract with.

Secretary Cook mentioned that the State had similarly long agreements with video lottery machine groups. The purpose of having such a long agreement was revenue sharing and to try to keep the cost down.

Senator Lavelle said that this contractual agreement has been in place since 2001. In the years since then, he would have expected there to be competitors in the field developing. He believes that this competition should allow the State to find a better price for these audits.

Secretary Cook said there was analysis done of what the major accounting firms charge for this type of service and that amount has been used as a benchmark. The rates have gone up over the past several years, but the long contract the State has with Kelmar has helped keep the costs lower.

Mr. Ratledge said that he thought that if Kelmar was not using proper accounting procedures that a holder would have sued them by now. He asked how Kelmar accounts for changes in a company, such as IBM, in an estimation looking back when they are working with forward-looking data.

Mr. McQuillen said that they start by looking at revenue and then make adjustments for companies that have been acquired or have spun off. They then look at the nature of the companies acquired, such as where they are located; since Kelmar has no contract with Alaska those records might be excluded while records pertaining to California and Delaware would be included. It is a regressive view of the economic history of the company. In some circumstances, such as payroll review, it is possible to review the 10K's and get the historic payroll records. The criteria that Kelmar is instructed to use to decide which data to use is that it has to be historic, determinable, and as close as possible to the economic stream that they are trying to measure. The statisticians try to do aggressive curves rather than a flat line backwards, since that would give a more accurate historical picture of the company.

Ms. Whitaker said that if the holders have a problem with the way the auditor is doing the audit they can contact her. If they have an alternate way to suggest for doing the audit her office is open to considering that.

Mr. Ratledge said that there is an assumption that company recordkeeping is improving and that the

unclaimed property field is consistently increasing. A lot of businesses that go out of business are small businesses that are probably being run on the proprietor's credit card. It is important that they get their money back.

Senator Townsend said that he would be interested in hearing from groups that represent small businesses in order to hear the small business perspective on this issue.

Ms. Whitaker said that companies that are concerned about the long look-back system have the option of joining the VDA program.

Mr. Lindholm said that companies that are already

undergoing audits do not have that option.

#### PUBLIC COMMENT

There was no comment from the public.

Senator Townsend thanked the Task Force members for attending and for their comments. He then informed the members and the public of the next Task Force meeting, which will be held on Thursday, October 2, 2014 from 1:30 p.m. – 3:30 p.m. at Buena Vista. The Senator also informed them that there would be an additional meeting on Tuesday, October 28, 2014 at Legislative Hall in Dover at a time to be determined.

The meeting was adjourned at 5:40 p.m.

## Minutes of the Meeting of the Unclaimed Property Task Force of Thursday, October 2, 2014

Buck Library, Buena Vista State Conference Center, 1:30p.m. – 3:30p.m.

#### Meeting Attendance – Task Force Members Present:

Senator Bryan Townsend  
Senator Greg Lavelle  
Secretary Jeffrey Bullock  
Thomas Collins  
Edward Ratledge  
Stan Stevenson  
Robert Tuinstra, Jr.

Representative Bryon Short  
Representative Jeff Spiegelman  
Secretary Thomas Cook  
Michael Houghton  
Jordon Rosen  
Leonard Togman  
Michael Barlow (newly-appointed representative of the Governor's Office)

#### Absent:

Controller General Michael Morton

#### Staff:

Michelle Zdeb  
Alton Irvin

Kathryn "Kiki" Evinger

#### Attendees:

Jamie Johnstone, DOF  
Courtney Stewart, CGO  
Rebecca Byrd, Byrd Group, LLC.  
Rick Gisenberger, DOS  
Freda Pepper, Keane, Inc.  
Michelle Whitaker, DOF

David Gregor, DOF  
Caroline Cross, DOJ, representing DOF  
Ferdinand Hogroian, COST  
Deb Zumoff, Keane, Inc.  
Alison Iavana, DOS  
James Dechene, DSCC

The Task Force Meeting was brought to order at 1:45 p.m.

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#### CONSIDERATION OF MEETING MINUTES, SEPTEMBER 10, 2014

Senator Bryan Townsend, co-chair, thanked the members of the Task Force and the public for attending the meeting. He addressed the first item on the Agenda: Consideration of the previous Meeting's Minutes. He apologized that the minutes from the previous meeting were only distributed with one day's notice. In order to give the members of the Task Force time to review the Minutes, the Minutes will be approved at the next meeting.

#### PRESENTATION BY DEPARTMENT OF FINANCE (DOF)

Secretary Thomas Cook, DOF, said that DOF would like to use this opportunity to answer some questions that Task Force members had asked in earlier meetings. There had been a lot of discussion in the previous meeting about the exact meaning of the 8% figure that Kelmar had mentioned in their presentation. Approximately 24% of total revenue from Delaware's abandoned property program is generated from the general ledger audits. Approximately 40% of that 24% is generated through estimation in those general ledger audits. The amount of estimation as a percentage of the total (24% x 40%) is 9.8%, which is approximately the figure that Kelmar gave.

Michael Houghton, Uniform Law Commission, asked if that would mean that, for example, if the total amount of revenue derived annually from unclaimed property in its aggregate was \$500 million, that approximately 24% of that (\$125 million) would be general ledger audit and only 10% (\$12.5 million) of that is the consequence of estimation.

Secretary Cook said that the chart in his presentation used FY 2008 – FY 2013 as base years.

Mr. Houghton asked if that meant that a lot of what the Task Force was talking about, including the look-back period and reasonableness of estimation, in his hypothetical was a \$12.5 million argument.

Senator Townsend requested that someone check the math on the figures presented in the chart, since he believed they were incorrect.

Mr. Houghton asked if the 10% was 10% of the total amount or of the 24% related to general ledger audits.

Senator Townsend said 40% of the 24% was a result of estimation, or approximately 10%.

Jordon Rosen, Delaware State Chamber of Commerce (DSCC), said that there were amounts being given in percentages and dollar amounts. He was not sure if these referred to the number of audits or dollars generated by the audits. Those are two very different things. He asked if the percentages referred to dollars or the number of audits.

Mr. Houghton said that it was the total amount of revenue generated by audits in the general ledger. There are of course audits that relate to other sources, such as equities and dividends.

Secretary Cook said that in securities there is no estimation.

Mr. Houghton said that the total amount of revenue generated as a result of audits is more than 24% of the total because a not insignificant portion of that was the function of audits related to equities.

Deputy Secretary David Gregor, DOF, said that the chart only refers to general ledger audits.

Senator Townsend asked for clarification that of all the money related to Delaware's unclaimed property program, 24% is from general ledger audits.

Deputy Secretary Gregor said that was correct.

Mr. Rosen asked that if there were dollars instead of percentages (and if the total was \$500 million) that the 9.8% would be roughly \$50 million and the 24% would be \$125 million.

Deputy Secretary Gregor said that was correct.

Senator Townsend asked if, using the \$500 million example, approximately \$50 million would relate to estimation.

Deputy Secretary Gregor said that was correct.

Mr. Togman stated that these numbers are not an average, but rather an annual total.

Senator Townsend said that was a good point. He asked if those numbers were relatively consistent over the years or if estimation has been increasing or decreasing.

Deputy Secretary Gregor said the dollar amounts change a lot from year to year but that estimation has been pretty consistent.

Senator Townsend said there are two layers to this discussion, one being the percentage of all revenues related to general ledger audits and the second being in general ledger audits what percentage is related to estimation versus non-estimation. He asked if the 10% is consistent over the years.

Deputy Secretary Gregor said the 40% is consistent. There could be years for which the general ledger percentage was 15% and others for which it was 50%. On average, over the six-year period, it was 24%.

Senator Townsend asked if there were any trends in this data.

Mr. Rosen asked what percentage did general ledger audits constitute in 2012 and 2013.

Deputy Secretary Gregor said in 2013 it was approximately 35% of revenue.

Mr. Rosen noted that would mean that estimation in 2013 would have been closer to 15%.

Mr. Togman asked if the Task Force could be provided with the totals broken down by years.

Deputy Secretary Gregor said that the Task Force should have already received that information. The 24% figure will change from year to year depending on

how many audits are conducted. The percent of general ledger examination from estimation (40%) is relatively constant.

Senator Townsend said that there is nothing wrong with averaging, but he wanted to know if there were any trends in the data that were disguised by averaging.

Deputy Secretary Gregor said he did not think there were any identifiable trends.

Robert Tuinstra, Jr., Delaware Business Roundtable (DBR), asked how much money was coming from estimation in general ledger audits. Is that the 40% and is that stable.

Deputy Secretary Gregor said that Mr. Tuinstra was correct and that it was stable. Equity examinations would be set aside and put in a different category.

Mr. Tuinstra asked if the equity examinations use estimation.

Deputy Secretary Gregor said they do not.

Secretary Jeffrey Bullock, Department of State (DOS), said that the holders he works with in the VDA program welcome estimation because it saves them money.

Mr. Togman said that there are many holders who do not feel that way.

Mr. Houghton said that the people that Secretary Bullock works with in the VDA program are in a managed process where the benefit of many presumptions are taken by them in their favor in the course of quantifying liability. It does not mean that it is not a credible program, but it does mean that by its design that it is intended to be collaborative and cooperative. He said the consequence of extrapolation and estimation in the VDA context is not as severe as it would be if the company was not in the VDA. It is fundamentally different in its result. If it was not, 713 companies would not have joined the VDA program. Mr. Houghton believes that many companies would not view estimation favorably if \$40 million - \$100 million are the result of estimation in a year derived from general ledger audit. Holders may view estimation differently depending on whether they are in the VDA

program or not.

Secretary Bullock said that how estimation is viewed is in the eye of the beholder. It has less to do with estimation and more about the audit process.

Mr. Houghton said that it has everything to do with the result of estimation. He would contend that holders that go through the VDA program, even in a situation where estimation is used, pay significantly less to the State of Delaware than they would if they had gone through the audit program. There are many people in the holder community who say that is the way it should be; the Secretary of State's VDA program, even with estimation, is a more realistic assessment of what the liability is. Mr. Houghton thinks is more about the result than the methodology. If someone goes through the VDA program and pays \$1 million but if they went through an audit they would pay \$11 million, then estimation is really irrelevant if the consequence is that they are paying \$10 million less.

Secretary Bullock agreed that it was less about the methodology and more about the result.

Secretary Cook said he wanted to clarify that the holders are part of the discussion when the base years for extrapolation are being selected. At the last Task Force meeting, there was some concern about the methodology that audit companies were using. Mr. Ratledge met with auditors that work for Kelmar and can report to the Task Force about his findings.

Edward Ratledge, public member, Director of the Center for Applied Demography & Survey Research (CADSR) at the University of Delaware, said when he met with Kelmar he asked to be walked through the audit process, such as the sampling procedures and how the final estimate was calculated. Some of the data showed remarkable changes from one period to the next. New accounting systems after Y2K showed an increase from few reports of abandoned property to large amounts of abandoned property. The conclusion he reached from that trend is that companies were significantly underreporting or did not know, and that it is difficult to tell which.

Mr. Ratledge said there are many instances where the holder gets to negotiate with Kelmar auditors on the measures that are being used. Sometimes they make the

wrong choices for their company, but they are still given that opportunity. There were opportunities to challenge items that had been found within their records and have those eliminated from the calculations. There is a final stage where the stratified sample is taken from the total number of items and research is done on those items. Even after that, the holder has an opportunity to negotiate whether the items should be included. The final step is when the auditors do the look-back on a particular section, like annual revenues in the past twenty years, and examine the relationship between the periods for which there is no data and the periods for which there is good data. The measure in that case is also negotiable.

Mr. Ratledge said that he could see nothing wrong with Kelmar's methodology. The data is largely based on data after Y2K, so the measures are very good. The results between the Secretary of State's VDA program and the DOF audit program will be different, particularly since the look-back in the VDA program is limited to 1996. The intensity is different. Mr. Ratledge said that when he spoke with Kelmar's statistician and one of their auditors he agreed with the way they performed the audit.

Michelle Whitaker, DOF, said that she agreed with Secretary Bullock that there are holders that recognize that they have an obligation to file and are compliant with the process. The majority do not. Some holders have thanked Ms. Whitaker and her team after an audit. She said this indicates that there is a level of professionalism shown by DOF and auditors. Ms. Whitaker said she is willing to negotiate with holders if there is a measure they do not agree with. She does not think that all holders are necessarily trying to get out of their obligations.

Secretary Cook returned to his presentation. He said that in the previous fiscal years, DOF has returned \$15 million - \$20 million to owners. In FY 2014, that amount significantly increased to \$104 million paid (\$46 million in cash and \$58 million in pre-liquidated shares). This is because DOF has been focusing on improving their due diligence and sending out more letters to claimants notifying them of their property.

Senator Townsend asked why there was a change in policy in not liquidating the shares.

Secretary Cook said DOF found that assets were being turned over to them without proper due diligence being done by the holders. The goal of the program is to return property to the rightful owner. By engaging in more due diligence, the State is able to accomplish that goal more often. This is an ongoing policy. Previously, DOF used to liquidate shares thirty days after they were turned over to the State. There was an assumption that the holders had already done the due diligence. When it was found that was not the case, DOF increased its due diligence.

Senator Greg Lavelle said there was a tremendous difference between the amount of claims paid in FY 2014 and in the FY preceding that. It seems like the consumer got the short end of the stick for quite a while. He asked why companies were just turning over their unclaimed property to the State without performing due diligence.

Secretary Cook said that answer relates to the U.S. Supreme Court's (SCOTUS) decision that the property does not belong to the holder. It does not matter to the company which state gets the property since they know they are not allowed to keep it. It is easier for holders to send the property to the State and have the State do the work of doing due diligence.

Senator Lavelle said that either people who were supposed to get property in FY 2013 and before did not, or people who were not supposed to get it did in FY 2014.

Secretary Cook said one thing to keep in mind is that the State will return the property if the claimant has the proper documentation, whether that is after two years or 25 years.

Senator Townsend asked how much revenue came in after the recent developments relating to transfer agents. Could some of the numbers in the chart be elevated because of that.

Secretary Cook said that it was \$195 million and agreed that some of the numbers could be elevated for that reason.

Deputy Secretary Gregor said that it looks like the rate of cash returned will be approximately the same rate this year.

Secretary Cook said that it is important to keep in mind that it is the responsibility of the holder to turn over unclaimed property to the State. The State made the assumption that the holder has done due diligence and made attempts to reach out to the owner.

Deputy Secretary Gregor said that if DOF had not had someone look at the transfer agency books and records, this lack of due diligence on the part of the holder would not have been discovered. Through the course of that investigation, hundreds of millions of dollars were switched from inactive status to active status.

Stan Stevenson, Delaware State Bar Association (DSBA), asked if the spike in cash is all related to the dividend property type that came in as a result of the examination of the transfer agency.

Deputy Secretary Gregor said that may have contributed some, but he thinks the spike in cash is more likely due to DOF using better methodology and processing methods.

Mr. Houghton asked if the \$46 million in cash was going to Delaware residents.

Deputy Secretary Gregor said no, about half of that amount was going to foreign (non-U.S.) addresses.

Mr. Houghton asked if the remaining half was going to Delaware residents.

Deputy Secretary Gregor said some part of that would, but he was not sure what the exact number was. If the State receives unclaimed property and the last known address is in Alaska, they send it there.

Mr. Houghton said he understood that, but he wanted to point out that although it is great that DOF is increasing its consumer protection, but he did not want the Task Force to think that means \$104 million is being returned to Delaware citizens. The overwhelming amount of that is not. He questions why the State is receiving money that has addresses in other states or in other countries since the laws of escheat provide that it be returned to the state of the last known address. The State might say that at the time it is remitted to them there was no address associated with the property. Subsequent research allows the State to investigate where

the property should be sent. Mr. Houghton advises his clients against sending money to a state if there is an address which sources the money somewhere else. He guesses that Delawareans are receiving less than 10% of the \$104 million paid in claims in FY 2014.

Deputy Secretary Gregor said that the money goes to the last known address of the holder. If a college student at the University of Delaware has an account and then ends up working in Wisconsin, the last known address is in Delaware. If someone notifies the student that they have this property and they file a claim, the State of Delaware would end up sending that money to Wisconsin because that is the address of the rightful owner.

Senator Townsend asked what the process is for returning property if the owner is found to live in another state. He asked if the check is simply sent to the last known address and the State waits to see if it is deposited or returned.

Deputy Secretary Gregor said no. The owner has to file a claim and establish that they are the rightful owner.

Senator Townsend said that he received Facebook messages from a woman in California who was very frustrated with the amount of time it was taking her to get the proceeds from a stock sale. It was very clear that once the stock had been sold, the proceeds should have been remitted very quickly- not after a lengthy waiting period and not a check by U.S. mail. Legislators do hear from constituents who are concerned about this process. It is good to know that there is a focus on improving the customer service aspect of this process.

Senator Lavelle said that there seems to have been a change in methodology between FY 2013 and FY 2014 that improved returns. He said that this is proof that processes can change to be more fair and equitable for everyone. He thinks that these processes need to be looked at from time to time to make sure that the State is not the only one benefitting from them.

Secretary Bullock said that estimation can work very well in some contexts and not in others. It is important to be very careful with estimation. Secretary Bullock said that he agreed with Senator Lavelle that changing this process was a reaction on the part of DOF to criticisms. That is excellent.

Senator Lavelle suggested that this idea of reacting to criticism to improve systems and services is one that could be applied to this Task Force.

Tom Collins, Delaware Bankers Association (DBA), asked if the change in DOF's policy regarding processing and distributing shares is a change they will maintain in the future.

Secretary Cook said that they would.

Mr. Collins asked if the State was going to become the registered holder of those shares.

Secretary Cook said that in the past when the State received escheated shares they used to be liquidated within thirty days. If an owner was identified after the shares were liquidated they were given the funds that were received from the sale of the shares. The concern was that not all holders were performing due diligence to find owners. Now when the shares are escheated to the State, the State sends out two letters to try to find the most updated address (sometimes using tax records) of the owner. If the owner does not contact the State to claim the property within 60 – 90 days, then the shares are liquidated. If the owner is identified after that time and they want the shares back instead of the liquidated cash, the State would have to buy back the shares for them.

Mr. Togman asked what would happen if the shares were in a brokerage account.

Secretary Cook said that DOF attempts to contact the owner through the last known address. They also look at tax records.

Mr. Togman asked if the shares were in a Merrill Lynch brokerage account if the shares would go back to them and they would be responsible for finding the owners.

Deputy Secretary Gregor said he was not sure about the specifics of that particular situation, but he could find out that information.

Senator Townsend asked what kind of standard is there or should there be with regards to holding shares. He asked if there is any kind of fiduciary standard. It is likely that there have been people who were upset that

the shares were liquidated. He asked if other states have different procedures.

Deputy Secretary Gregor said that after due diligence it is standard practice to sell the shares immediately so there are no accusations that the State is trying to influence the stock market.

Mr. Houghton said other states, particularly California, have been sued for taking shares into escheat, disposing of them in the marketplace, and then the owner of the shares claiming that due diligence was not done. He thinks that this is a topic of general discussion around the country. Corporate America is looking for clarity in the rules of remitting and tendering shares to the State as well as the time period for selling them. Delaware has been responsive in this particular interest to the concerns of the equity community. There is no longer the thirty-day liquidation of shares. This influx is a result of a change in the law. The spike in the equity issue and the amount of money being remitted is a function of an enforcement mechanism put in place by the State in the last 2 – 3 years on equity that is now going to trail off. Mr. Houghton does not think this spike will be seen again. He believes the equity revenue is going to level off and become a more a more consistent level than it has been.

Senator Townsend asked if it was going to be at a higher level than it was previously.

Mr. Houghton said he is not sure if it will be significantly higher. It was a backlog of reporting that had not been done for 20 – 30 years, and now many people are not in compliance historically but will be in the future. It is probably going to be slightly higher in equities.

Deputy Secretary Gregor said that it might be slightly higher but it depends on a lot of factors.

Mr. Houghton said this was similar to what James Hartley from Verus Financial mentioned in his presentation at the last Task Force meeting about insurance audits. They are not relevant to the State of Delaware because it is all addressed property, but there was a long period of time when there were amounts that should have been tendered as unclaimed property. Once that area has been cleaned up, the industry will get into a rhythm of returning property and there will

be less revenue for the State. It seems as though there is something new every 3 – 4 years in equities; it is a cycle. The State has done some positive things in the way they have reformed the disposition of shares.

Deputy Secretary Gregor said regarding the \$58 million in shares, the State did not liquidate it so it was never declared as revenue. This was a customer service that does not count as revenue.

Mr. Togman asked what happens to the dividends on those shares while the State is holding them.

Deputy Secretary Gregor said if the owner asks for the dividends the State returns them.

Senator Townsend asked what happens if the owner does not ask for the dividends.

Deputy Secretary Gregor said in that case the State keeps them. If there is no claim made for the assets they are not returned.

Senator Townsend said if there is a claim made for the shares and not the dividends that could indicate that there is an address for those dividends as well.

Deputy Secretary Gregor said there used to be some system limitations that prevented that connection from being made, but it is something that DOF would be willing to work on if the Task Force makes that recommendation.

Senator Townsend asked if there was any sense of what the value of those dividends would be.

Deputy Secretary Gregor said he did not know.

Senator Townsend referred to DOF's figure of \$58 million in shares returned in FY 2014. He asked if that was measured by a certain date they were returned or what the market value was when they were escheated.

Deputy Secretary Gregor said that the figure was based on the value of the shares either on the day the State received them or on the value the day they were returned.

Mr. Rosen said it might not matter which day was used because it was not being counted as revenue. If dividends were approximately 2% of the shares and

the total was \$58 million, then the dividends could be worth \$1 million.

Mr. Collins asked if the owners had to make a claim expressly for the dividends or if they were included with the shares.

Deputy Secretary Gregor said that it has been a case-by-case situation. There have been system limitations but they are updating to a new system, which should make connecting owners of shares with the dividends easier.

Mr. Togman asked what the length of time that the State keeps shares while doing due diligence is before the shares are liquidated.

Deputy Secretary Gregor said that it is 60 – 90 days from the time that the owner should have received the due diligence letters. If the last known address is in Delaware, DOF holds onto the shares for a longer period of time before liquidating them.

Senator Lavelle asked if there is a dividend with a share if the State keeps it. Is the State aware that the dividend for the share exists.

Secretary Cook said yes.

Senator Lavelle said that does not seem fair. If the premise of this program is to return money that does not belong to the State, then not sending the dividend with the share to the owner does not fulfill that premise.

Senator Townsend said it seems like there were some systemic limitations that prevented DOF from returning the dividends with the shares. It is good to know that they now support an automated service to return the shares and the dividends together to the owner.

Secretary Cook returned to his presentation. He explained what the State is looking for when it hires contract auditors. One of the main things that holders are concerned about is confidentiality. They want to make sure that when they interact with auditors that all information will be kept in confidence. The holders look for predictability and properly documented and clear findings. It is important that auditors have in-house expertise and capacity, such as a good IT infrastructure.

They must also have legal support and a detailed statistical sampling method.

Mr. Houghton asked why contract auditors would need to have legal support since the State already has attorneys to advise them. He is not sure why that would be a predicate to hiring an auditing company, because they would be dealing with Delaware law which State attorneys could advise on.

Secretary Cook said that he thinks that contract auditors do need that experience because they work in multiple states. The DOJ gets involved in different kinds of dispute. Companies like Kelmar need to have a background in Delaware law if they are going to be working in Delaware.

Mr. Houghton asked if Secretary Cook meant that an auditing company would have to understand the rules of Delaware, including that they would not be allowed any substantive decision-making power during the audit.

Secretary Cook said that is what he meant, and that in the last meeting Kelmar and the State had made it clear that the auditing companies do not have decision-making power in the audit. The State makes all final decisions.

Secretary Bullock said that there are many issues that are a matter of interpretation in an audit. If the State had to ask the Attorney General's Office for every one of those issues, they would have to have three or four more Deputy Attorney Generals (DAGs).

Mr. Houghton said that there probably should be more DAGs assigned to an area that is a \$600 million revenue source.

Secretary Bullock said perhaps that is true, but it would cost a lot of money. There are parts of the audit that require negotiating, and lawyers tend to be good at that.

Mr. Rosen asked if the State has a contract auditor "best practices" manual that includes the selection process of contract auditors, criteria that auditors must meet, and the steps of the audit process.

Secretary Cook said that a lot of that information

was already laid out in the contracts the State has with contract auditors.

Mr. Rosen said he has seen the contracts and contracts are negotiated.

Deputy Secretary Gregor said that they are often boilerplate contracts.

Mr. Rosen said that the two contracts he looked at were boilerplate contracts, but that parts of them were negotiated. He asked if there is a manual that lists the standards the auditors must meet in order to be considered as a contract auditor for the State.

Deputy Secretary Gregor said that he has been the State Escheator for a little over a year. When he became State Escheator there were already many contract auditors working for the State. One of the first things he did was make a list of best practices, business philosophies, and expertise. All contract auditors were brought in to make a presentation and to discuss every item. It was made clear that any contract auditor that wanted to continue working for the State had to meet those standards. This list was never published, but it let auditors know what the State expected from them in terms of professional conduct and work product.

Mr. Rosen said that he thinks a best practices guide for auditors and the audit process would go a long way to show fairness.

Secretary Cook said that other states have done something similar to that and that holders have found that helpful. He said that one of the outcomes of this Task Force could be to publish a best practices manual.

Mr. Stevenson said that he is concerned that Kelmar is getting the majority of the auditing cases. He guessed that Kelmar is also being assigned the most lucrative audits as well. Mr. Stevenson asked if there was anything in this field that is precluding competition from other auditing firms.

Secretary Cook said that the chart on the "Diversifying Enforcement Support" slide showed how many cases were assigned in the past two fiscal years to each of the five auditing firms the State contracts with, for a total of 45 cases. They have been focusing on auditing the companies that did not sign up for the

VDA program.

Ms. Whitaker said that they are focusing on companies (not all large companies) that are not a part of the VDA program. There is a wide range of company sizes.

Representative Bryon Short asked Ms. Whitaker to be more specific about the types of companies she was talking about.

Ms. Whitaker said that the companies are not "mom and pop shops," but that they are not all Fortune 100 companies either. They all are valued at over \$1 million.

Secretary Cook said that the chart also listed the number of employees each contract auditor employs. Kelmar has 147 employees that do audits and also have approximately another fifty employees who are support staff.

Senator Townsend asked if this was the number of employees who work on Delaware audits or the total number that work at the auditing firms.

Secretary Cook said that it was the total number of employees at the firms.

Senator Townsend said that puts why the State gives so many more audits to Kelmar in context- they have more employees and can handle the higher caseload.

Mr. Stevenson said that he does not think this slide is representative of the last eight years. It has been a very lucrative business for Kelmar. Normally in this instance you would see real competition from other auditing firms.

Deputy Secretary Gregor said that Xerox is an audit firm that specialized in equity audits. They used to have a very significant audit presence and they are in the process of rebuilding that. Kelmar is the gold standard in the audit field. Xerox has lost employees to Kelmar. The State would like there to be more competition in the field, but the State only hires contract auditors that only represent states, rather than those who represent both states and holders.

Senator Lavelle said that Kelmar received about \$50 million dollars in their contract. He asked which

auditing firm earned the next-highest paycheck.

Deputy Secretary Gregor said that year it would probably have been Specialty Audit Services (SAS) and they would have received a paycheck in the single digit millions.

Secretary Cook said that year was also the year of the transfer agency project. Kelmar brought in over \$400 million in revenue.

Mr. Houghton said that there have not been a huge number of new audits started by the State of Delaware in the past year. He asked what the total number of audits in their entirety assigned to Kelmar. Statistically, audits can last anywhere from three to eight years, sometimes longer. What is the total number that each of the firms listed has in the queue. It seems as though FY 2013 and FY 2014 were relatively slow years in terms of auditing, yet Innovative Advocates did not exist 18 months ago.

Deputy Secretary Gregor said that Kelmar has approximately 300 cases at the moment and there are a total of approximately 375 audits being conducted.

Mr. Ratledge said that after speaking with Kelmar auditors, he wonders how anyone could do this job with the subsidiaries that are involved with some of the large companies without having a large and experienced staff. It is very clear that this area requires a lot of experience and expertise; it is not easy.

Senator Townsend said that he is aware of the irony of some of the comments that have said the large size of Kelmar is a bad thing, whereas normally growth and success would be looked at as a good thing.

Mr. Tuinstra confirmed that there are 375 open audits that the State is conducting and that 300 of them have been assigned to Kelmar.

Secretary Cook said that is correct.

Senator Lavelle said that it is important to grow the audit service industry in order to drive down prices so that the State could save money and not be so reliant on certain audit firms.

Mr. Houghton said that he thought that he heard someone say that these auditing companies do not want

to grow. He said that is not the case. Companies would grow if they knew there would be a guaranteed stream of work that would support their infrastructure. It is like any business: they grow proportionally to the amount of work they have or foresee having in the future.

Deputy Secretary Gregor said that what the State has tried to do in the past couple of years is gauge the amount of work companies can handle right away. The State would like to give the smaller auditing firms more cases, but the State also has to be sure that it is getting the kind of work product it wants. Small businesses sometimes have growing pains as they are starting out. The State does not want the smaller firms to be overwhelmed, but they are parsing out cases differently than in previous years. Kelmar has three-quarters of the cases, but in the past couple of years has only received half the cases. The State is making efforts to spread the work out more.

Mr. Houghton said that Kelmar in the past five years has expanded from representing 12 – 15 states to representing over thirty. They are providing audit services and a significant amount of IT support. They are modifying their model because Kelmar is anticipating that the workload from Delaware is going to decline. If Delaware is going to maintain a credible audit business it will have to diversify the number of audits it gives to others.

Mr. Ratledge said that part of the purpose of his visit with Kelmar employees was to determine if they are applying estimation and extrapolation arbitrarily. They have to ground their decisions in policy or law. Kelmar had the right answers, but that does not mean that other firms would not also have the right answers.

Secretary Bullock said that he interprets this chart in the same way he interpreted DOF's modifications to their due diligence practices: it is a change that is a reaction to criticism of DOF. DOF was told that too much work was being assigned to Kelmar and that the workload should be more spread out. As a result, DOF is trying to take a more balanced approach to assigning cases. If there is less of a reliance on audits, a lot of the problems being discussed (like estimation) would go away. He thinks that is what has been happening over the past 18 months.

Secretary Cook said that DOF is encouraging

companies to join Secretary Bullock's VDA program. This makes annual filings and revenue more predictable.

Deputy Secretary Gregor said that there are more than twice as many companies in the VDA program as there are under audit.

Mr. Rosen said that he agreed with Secretary Bullock. It is better to have voluntary compliance than to have to rely on audits. He asked why the State has not considered adding, on a gradual basis, a qualified audit unit within the State. The State could be its own vendor.

Secretary Cook said that is something that has been discussed. The auditing companies are auditing large multinational corporations with many subsidiaries. The State does not have the expertise or resources to do those audits. The State has hired auditors in the past and they have left because they can get a higher salary in the private sector. DOF has discussed hiring auditors to perform some of the smaller in-state audits.

Mr. Rosen said he did not think that the State was going to compete with Kelmar for the reasons that Secretary Cook mentioned. If the State added on a small number of employees on a gradual basis to do some of the smaller audits then the State could save money.

Mr. Houghton said that there is precedence for this. When the Division of Revenue ran the VDA program it was staffed internally and it was successful. There is the historical capacity within the Division of Revenue to do reviews. There is no reason that capacity could not be expanded internally and applied to some extent to audits.

Senator Townsend said that he has been surprised to hear that State employees are burdens on the system and that they do not provide a benefit because he does not agree with that. He asked to hear some detailed descriptions of the types of tasks that could be assigned to in-house workers.

Mr. Ratledge asked what would be the change in revenue as a result of this. For example, the VDA program has been put into effect; what has been the net change as a result of that. Secretary Bullock had mentioned earlier that approximately 33% of companies that could have joined the VDA did. Mr. Ratledge questioned whether those companies would have joined if there was no

threat of auditing. Mr. Ratledge does not believe that unclaimed property would decrease as a result of the VDA program. Technology has been around for decades and unclaimed property is still increasing.

Mr. Tuinstra said that it is important to have a good audit program. He does not think that anyone in the business community is advocating that audits should be eliminated. A strong audit program also should have strong rules so that the methodology and rules are very clear.

Senator Townsend asked what types of tasks could be assigned to in-house workers.

Secretary Cook said that the VDA program recently ended and that the increase from that program is over.

Senator Townsend asked about the final results of the VDA program.

Secretary Cook said the legislation allowed companies to sign up for Secretary Bullock's VDA program. If companies signed up within the first year the look-back period was limited to 1996 instead of 1991. If they signed up by September 30, 2014 the look-back period was limited to 1993. Because that date has passed, no other companies can sign up for the VDA program. The look-back reverts back to DOF's 1991 look-back. On the audit side, the regulations changed the look-back period to 1986. It will stay at 1986 until June 30, 2015 when it will revert back to 1981.

Senator Townsend asked if there was an increase in enrollees and what the differences between the DOS and DOF VDA programs are.

Secretary Bullock said yes. In the past couple of days approximately 75 companies signed up. Companies cannot sign up for his VDA program any longer.

Ms. Whitaker said that the look-back period is different, with DOF's being 1991. She did not think the methodology of the two programs is significantly different. DOF's program is still accepting enrollees.

Mr. Togman asked for clarification of the look-back periods for each VDA program.

Ms. Whitaker said the Secretary of State's VDA

program had a look-back to 1993 and the Secretary of Finance's program had a look-back to 1991. There was some confusion in the industry about the two programs, so DOF changed their look-back period to 1993 to mirror the DOS VDA program.

Deputy Secretary Gregor said that there has been a perpetual amnesty program. This will always be open. Auditing companies that are noncompliant is important.

Senator Townsend said it has been established in previous meetings that no one has a problem with auditing companies that are deliberately in noncompliance.

Senator Lavelle said that he would not agree that the methodology of the DOS and DOF programs is the same.

Ms. Whitaker said that they are not identical, but that she would not consider them to be significantly different.

Senator Lavelle said that he realizes that there are differences in the look-back periods. Putting that aside, if he was a sneaky, mean company he could just sign up for the VDA and then not comply with the State.

Secretary Bullock said that it is a voluntary program. That works both ways. Companies that do not comply get kicked out. DOS also had a reputational advantage with this program; it has a good relationship with holders. DOS was also successful in marketing the program.

Senator Lavelle asked if the arrangements that DOS has with outside vendors is different than the ones DOF has with contract auditors.

Secretary Bullock said that it is, but the vendors are paid an hourly rate not a percentage.

Senator Townsend asked what the timeframe was for any type of analysis or report on the DOS VDA program. He asked what implications would there be on the audit system now that the DOS VDA program is closed.

Secretary Bullock said he thinks that there will have to be some kind of successor to the DOS VDA program,

although he is not sure what that would be. They have done all that can be done with the VDA program, so it would have to be a variation on that.

Senator Townsend asked if the DOF VDA program would serve as a long-term successor.

Secretary Bullock said that it has historically been the alternative to an audit, but it is hard to tell what will happen in the future.

Senator Townsend said he would be interested in seeing some analysis of the implications of this program ending and the audit and DOF VDA programs being in the same department. He again expressed his interest in hearing some detailed descriptions of the types of tasks that could be assigned to in-house State workers.

Secretary Cook said that he thought that in-house State workers could be hired to work in a limited scope. The biggest fear is that the State will invest time and money in training employees and have them leave to work in the private industry. The opportune time to do this may be during the transition period between the DOS and DOF VDA programs.

Senator Townsend asked if there were any specific tasks that could be assigned to State workers.

Deputy Secretary Gregor answered that those employees could work on the VDA. They would be reviewing the methodology that has already been put forth, rather than gathering the data in an audit.

Senator Townsend asked if the idea of using in-house workers was ever considered for the DOS VDA program.

Secretary Bullock said no, because the ramp-up for the VDA program had to be so fast. The DOS VDA program was a limited time program. There was not enough time to do the kind of staffing Senator Townsend described. If the DOS VDA had been a longer program, Secretary Bullock would have probably hired more staff. The task would have required highly skilled employees, which would have probably been expensive.

Senator Townsend said that he realized that as a result of companies joining the DOS VDA that there are a lot of audits in the pipeline. He asked if more in-house

State staff could be hired to help with that backlog.

Secretary Bullock said that they would only be able to be hired for a limited duration, since his program ends on June 30, 2016. Staff would only be hired for approximately twenty months.

Senator Townsend said that just because that particular program will end does not mean that the staff could not be reassigned to work on other projects. The expertise and skills developed during that time could be transferred to other tasks. This could save the taxpayers money.

Representative Jeff Spiegelman referenced Secretary Bullock's earlier statement that 75 companies had joined his VDA program in the last couple of days. He asked if he thought that was just a last-minute rush.

Secretary Bullock said that he thought it might be.

Representative Spiegelman asked if the DOS VDA program was extended if more companies would join.

Secretary Bullock said that because of the marketing that was done for this program, companies all knew about the VDA program. They chose not to join. He does not think more companies would join if the program was extended; there has to be something that is a little different.

Mr. Houghton said that several large companies contacted him in the past couple of days who were considering joining the VDA program. After looking at the cost, time, and effort it would take to join the program, they decided that it was not worth it. One of the problems that companies had with the Division of Revenue VDA was that there was an 18 month post-closure audit period. VDAs could be closed, but the State then had 18 months to audit the company for the same period. Mr. Houghton said he represented at least two companies that had that experience.

Mr. Stevenson said that the fact that the audit was a possibility was a reason why companies preferred the DOS's VDA program.

Mr. Houghton said that he is not sure that the Task Force will have sufficient time to develop a set of comprehensive recommendations.

Mr. Togman noted that if the Task Force does not make any changes that could impact Delaware's fiscal future. It could cause corporations to incorporate elsewhere.

Mr. Tuinstra said that a representative from the Council on State Taxation (COST) was present at the meeting and could offer insight into that issue from the perspective of holders. Secondly, he requested that the Task Force members receive some guidance as to how to proceed with their recommendations.

Secretary Cook returned to the presentation. He said that there are several important things to note about the contracts the State has with auditors. The State, not the auditing firms, makes all critical decisions related to the audit. Delaware is not the exception; all states use contractors. The reason why DOF has such lengthy contracts with auditors is because unclaimed property exams typically take years. Having a shorter contract would mean renegotiating with the contract auditor when examinations are only partially complete. Having a longer contract also locks in costs, but it does not lock in operations. The State has the prerogative to stop assigning cases or to reassign cases at any time.

Senator Lavelle referred to Kelmar receiving \$50 million last year. He asked how many hours they worked.

Secretary Cook said he could get that information for the next meeting.

Senator Lavelle asked what the highest payment was to a VDA member in 2013.

Secretary Bullock said that he did not have that information on hand, but he believed that the point Senator Lavelle was trying to make was that the cost of a VDA is less than that of an audit. That is true.

Senator Lavelle expressed concern that because the contracts are so long that qualified auditors would be precluded from being an auditor for the State.

Secretary Cook said that is not the case because DOF has a rolling RFP. The State can bring on new auditors at any time, not just every so often as would be the case with the normal RFP process.

Senator Townsend asked what the lengths of the

contracts were for other smaller auditing firms.

Ms. Whitaker said that Innovative Advocates' contract mirrors the length of Kelmar's. Specialty Audit Services (SAS) has continually requested two-year contracts and DOF continues to honor that request.

Senator Townsend said that the contract formalizes the relationship between the auditing company and the State; it does not guarantee what they get paid.

Ferdinand Hogroian, Tax & Legislative Counsel at COST, said that COST conducted a survey of its members as a reaction to some of the concerns expressed at the previous Task Force meeting. They wanted to substantiate some of the concerns that holders have. COST conducted an anonymous survey via Survey Monkey of the COST Unclaimed Property Committee (consisting of about forty members, some not Delaware-incorporated and not participating in the survey). This survey showed that members have a robust multistate filing history as well as a robust Delaware filing history. There is a comments section where members could expand on their concerns. The holders expressed concerns about estimation and the record retention period. Companies that responded also stated that they have had to pay over \$1 million in legal fees and staffing costs as a result of the audit, and that does not include the amount that the audit finds them liable for. Mr. Hogroian said that the reason why companies preferred the DOS VDA to the DOF VDA was because they knew they would not get audited after joining and there was clarity about the process.

Senator Townsend said that if that was true, why didn't more companies sign up.

Mr. Hogroian said that a lot of the member companies of COST are ineligible to sign up for the VDA program.

Secretary Cook asked how many members are in COST.

Mr. Hogroian said that there are over 600.

Secretary Cook asked why there were only responses from 14 companies.

Mr. Hogroian said that they sent the survey out

only to the members of the COST Unclaimed Property Committee. They did not want to spread the link to the survey around too widely because anyone could answer the survey questions. Mr. Hogroian urged the Task Force members to review the comments section, because those are unfiltered opinions from member companies. It would be very difficult for those people to represent their companies and express those opinions openly in person to the Task Force.

Senator Townsend thanked Mr. Hogroian. He referred to Mr. Tuinstra's earlier comment about the process of making recommendations. Senator Townsend noted that there is a decent amount of consensus between Task Force members on several topics, particularly in the consumer protection aspect. He noted the irony that the length of record retention is exceeded by that the dormancy period plus the statute of limitations. Companies are being authorized to shred records but the statute of limitations is still open. He would advocate shortening the statute of limitations so that it, plus the dormancy period, equals the length of record retention requirements.

Mr. Togman said another item that could be reviewed is the fairness of the appeal process.

Senator Townsend agreed that is something that could be discussed. He remembered someone at an earlier meeting stating that there could be a mutual selection of an arbitrator.

Mr. Tuinstra said that another aspect of that topic that should be discussed is that the Secretary of Finance can reject or modify the decision of the arbitrator. This process does not look fair to an outsider. There is no appearance of fairness.

Mr. Houghton said that has been the fundamental criticism of the process. The appeals process is potentially very lengthy process. He thinks that the appeals process can be tightened up. The appeals process has not been used very much, but that could be because it is viewed as cumbersome and unfair.

Mr. Tuinstra said that this process is not a normal administrative appeals process in terms of that step.

Michael Barlow, Chief of Staff in the Office of the Governor, said that he disagrees with Mr. Tuinstra's

comment. It is actually standard practice in other administrative procedures to appoint a hearing officer who makes a recommendation to a Cabinet Secretary. It is done this way because the concept of fact-gathering involves very intensive efforts. It can be questioned whether or not this process makes the most sense, but the fact is that there is a Chancery process that provides for the court to make a ruling. What Delaware does not have, by tradition, that some other states have is a robust administrative law judge. This independent hearing officer process is more common.

Mr. Tuinstra clarified his earlier statement to say that it is not a common practice in the tax world.

Mr. Rosen said that he would recommend that the Task Force make a recommendation about what the definition of abandoned property is and what property is subject to escheat. He also recommends that a best practices manual be published to promote the idea of fairness and transparency. In the tax profession, a lot of attention nationwide is being paid to how Delaware handles the unclaimed property issue.

Senator Townsend said that he is happy to further discuss the idea of a more concrete definition of unclaimed property but he is not sure that it will solve any problems in the business community.

Mr. Rosen said that he does not think that the Task Force can come up with a comprehensive list to solve all of the problems discussed. The General Assembly will have to be involved in legislating. There does need to be a framework in place for a starting point.

Mr. Togman said that he would like to know how much of the revenue from abandoned property is attributable to business-to-business transactions and gift cards. He would also like to consider what including those items as abandoned property does to Delaware's reputation. COST rates Delaware as a D- as compared to other states. There should be a discussion on whether or not including those items should be changed.

Mr. Rosen asked if there was a possibility that the Task Force report deadline could be extended to allow for additional meetings.

Senator Townsend said that legally, no. Practically, conversations could continue. It will have to depend on

how members feel about the final report.

Secretary Cook asked if DOF will have an opportunity at the next meeting to present some of the data that was requested at this meeting.

Senator Townsend said yes.

Mr. Houghton said that a limitation on the look-back be something that is considered.

Senator Townsend said that he does think it is ironic that companies are required to produce records for the past thirty years during an audit when the State of Delaware would not be able to produce their records from that long ago. However, most of the companies who are complaining about the look-back period are companies that are not in compliance at all. DOF is targeting large (\$1 million+) companies who do not have a history of filing, and the Task Force has agreed that companies who are not in compliance should be audited.

Mr. Tuinstra said that his response to Senator Townsend's statement would be that all of the comments from the COST survey were from companies who had filed and were still being subject to audits.

Senator Townsend said that it is very difficult to make major modifications to state law based on anonymous comments. There is nothing unfair or aggressive about that.

Secretary Cook said that he thought that COST would have brought in a member company that had completed the audit process and that was indemnified to talk about their experiences. DOF has responded to criticisms to try to make the process fair and equitable and that they will continue to make changes.

Senator Townsend said that he does not know that any legislator on the Task Force that has been contacted by specific companies about their experiences. He has heard from companies in reference to other aspects of Delaware law.

Senator Lavelle said that he actually was contacted by a company. He said that the company felt that the audit process was heavy-handed and unreasonable. They were so unhappy that they were considering

shrinking their business in Delaware.

Representative Short asked if the company that Senator Lavelle was referring to was on compliance.

Senator Lavelle said he did not know.

Mr. Stevenson said that in terms of compliance versus noncompliance, there are companies that have no contact with the State of Delaware other than the fact that they are incorporated there. They may not have been under obligation to file because they might not have any Delaware employees or vendors. If there is an audit there is no record that they have filed, but they have never been required to file. The State might say that they are noncompliant, but really the companies are unable to defend themselves because they have never filed. Mr. Stevenson said that he does not agree with the premise of estimation when non-Delaware items are included (total unclaimed property is estimated). He does not think that there is any specific instance that makes the process unfair; the premise the audit is based on is unfair. Mr. Stevenson would not think the company is noncompliant in this scenario.

Mr. Rosen said that there need to be clear rules about the statute of limitation policies and record retention policies.

Mr. Tuinstra said that Kelmar is auditing non-filers. They go back to 1986 to check if a company underfiles. That is part of the problem because a company may think that they have kept the appropriate records for the statute of limitations and then are not able to prove that they have not underfiled. He did not think that all of the audits Kelmar does are targeting non-filers.

Secretary Cook said probably not all of the 300 cases that Kelmar has been assigned are non-filing companies. However, in the past two years what DOF has tried to do is to focus mainly on non-filers.

Mr. Tuinstra said that companies could have filed, but the look-back is still to 1986 to see whether the company filed appropriately.

Deputy Secretary Gregor said that if a major Fortune 100 company only files every fifth year and only files insignificant amounts that would be something that the audit would investigate further. The company has filed

in the past, but their filing history indicates that they may be underfiling.

Mr. Tuinstra said that his point regardless of whether or not the company filed correctly, there is a statute of limitations that should be adhered to.

Senator Townsend said that Mr. Tuinstra's comment related to his suggestion earlier that the two time periods should match. Even if the time periods match there are still going to be situations where the look-back period is implicated. It is not fair to characterize the situation as a filer going through the pain of an audit. The filer is going through the pain of an audit because there is substantial evidence to support that they have dramatically underfiled in the past. It's a whole separate basis for characterization and sympathy. Senator Townsend said there is a lack of evidence to support that the people who are being targeted by audits are those who consistently file the correct amounts.

Mr. Houghton said that he would recommend that Task Force members think of the situation with a more pragmatic approach. The Task Force could stay the course, but he thinks the State will see more and more litigation.

Secretary Bullock said that DOF has made great improvements over the past couple of years. He does not think State courts would change the process. The Task Force is charged with identifying more areas of improvement. He said that the Task Force should wait to see the report and see if it reflects the ideas and tone of the previous discussions. It is unfair to suggest that there have not been changes to statutes made to reflect the changing world and the value of this source of revenue.

Mr. Collins said that there are changes and improvements being made, but this field is being used as a revenue source but it really is not the State's money. Whether or not collections will continue remains to be seen. Regardless of what is decided, whatever the State does needs to be predictable to the business community in order to retain corporate benefits. There should not be too dramatic of a deviation, it should be straightforward.

PUBLIC COMMENT

There was no comment from the public.

Senator Townsend thanked the task force members

for attending and for their comments. The next Task Force meeting will be held on Tuesday, October 28, 2014 from 10:00 a.m. – 12:00 p.m. in the Senate Hearing Room at Legislative Hall in Dover.

The meeting was adjourned at 4:04 p.m.

## Minutes of the Meeting of the Unclaimed Property Task Force of Tuesday, December 2, 2014

Buck Library, Buena Vista State Conference Center, 1:00p.m. – 3:00p.m.

Meeting Attendance–Task Force Members Present:

Senator Bryan Townsend  
Senator Greg Lavelle  
Secretary Jeffrey Bullock (Via phone)  
Thomas Collins  
Edward Ratledge  
Stan Stevenson  
Robert Tuinstra, Jr.

Representative Bryon Short  
Representative Jeff Spiegelman  
Secretary Thomas Cook  
Michael Houghton  
Jordon Rosen  
Leonard Togman  
Michael Barlow

Absent:

Controller General Michael Morton

Staff:

Michelle Zdeb

Kathryn “Kiki” Evinger

Attendees:

Arsene Aka, DOF  
David Gregor, DOF  
Caroline Cross, DOJ representing DOF  
Ferdinand Hogroian, COST  
Rick Geisenberger, DOS  
Michelle Whitaker, DOF

Jamie Johnstone, DOF  
Courtney Stewart, CGO (Via Phone)  
Bob Byrd, Byrd Group, L.L.C.  
Sara Lima, Reed Smith  
Alison Iavana, DOS

The Task Force Meeting was brought to order at 1:09 p.m.

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### INTRODUCTION AND CONSIDERATION OF SEPTEMBER 10, 2014 MEETING MINUTES

Senator Bryan Townsend, co-chair, thanked the members of the Task Force and the public for attending the meeting. He addressed the first item on the Agenda: Consideration of the Meeting Minutes.

Representative Jeff Spiegelman motioned to approve the Minutes.

Jordon Rosen, Delaware State Chamber of Commerce (DSCC), seconded the motion.

The Meeting Minutes were approved, with all members in favor.

CONSIDERATION OF MEETING MINUTES,  
OCTOBER 2, 2014

Senator Townsend said he had received some requests for edits via email. He will recirculate these minutes and the minutes from today at a later point for Task Force members to approve.

CONSIDERATION OF DRAFT REPORT

Senator Townsend said that before the Task Force discusses the Draft Report, Deputy Secretary Gregor would like to clarify some data that Department of Finance presented at the previous meeting.

Deputy Secretary David Gregor, Department of Finance (DOF), referred to the "Task Force Findings" section of the Draft Report, bullet point number nine, referring to estimation of companies' liability. This point states, "Estimation of companies liability for past years' unclaimed property accounts for approximately 10% of Delaware's total annual unclaimed property revenues." Deputy Secretary Gregor stated that the percentage should be 20% instead of 10%. At the previous meeting when he said that 40% of audits were due to estimation, that number also included securities audits as well. The period of time that was examined was FY 08 to FY 13.

Senator Townsend asked if this number was the average over those six years.

Deputy Secretary Gregor said yes. Some years were lower, some were higher.

Senator Townsend said that he had asked at the last meeting whether there was any identifiable trend over that period of time. Is there a trend evident now.

Deputy Secretary Gregor said that he did not see any particular trends during those years. FY 13 was a peak in terms of general ledger audits. FY 14 was far below that. They are expecting some sort of a rebound for FY 15. He does not think the peak of FY 13 will be repeated anytime in the near future.

Mr. Rosen asked what the value was for FY 13 and what it dropped to in FY 14.

Deputy Secretary Gregor said that in FY 13 the value was approximately \$218 million. In FY 14 it was

approximately \$65 million.

Edward Ratledge, public, University of Delaware Director of the Center for Applied Demography & Survey Research (CADSR), asked if estimated abandoned property counted for 20% of \$600 million.

Deputy Secretary Gregor said yes. The numbers bounce around depending on the year. Some years there was a larger amount of revenue from securities audits. Other years were low; revenues were down last year.

Michael Houghton, Uniform Law Commission (ULC), asked if the figure Deputy Secretary Gregor mentioned was a combination of general ledger and securities audits.

Deputy Secretary Gregor said no. Originally, that was where the mistake occurred, when he gave the wrong percentage at the previous meeting. Of the general ledger audits, roughly 80-85% is due to estimation. That number changes a lot over time. Over the six year period that he sampled, the percentage averaged out to 20%.

Senator Townsend clarified that 20% of total revenues from FY 08 - FY 13 would be due to estimation.

Deputy Secretary Gregor said that was correct.

Robert Tuinstra, Jr., Delaware Business Roundtable (DBR), asked if the 80-85% of general ledger audits that use estimation was consistent.

Deputy Secretary Gregor said yes.

Mr. Rosen asked if it was 20% of all audits.

Deputy Secretary Gregor said that it was 20% of all revenue. In a year where there are very few securities audits, the percentage may be higher.

Mr. Rosen said in FY 13 there was roughly \$670 million, but there was approximately \$200 million from compliance, not audits. He asked for clarification on Deputy Secretary Gregor's figures.

Deputy Secretary Gregor said that was only one year. In FY 13 there was \$220 million in annual filings from cash. There was \$220 million in general ledger audits. There were Voluntary Disclosure Audits (VDAs)

of \$42 million and \$192 million as a result of an audit of transfer agents.

Mr. Rosen said that Deputy Secretary Gregor said that 20% of all revenue was from estimation; however there would be no estimation in a company that files a report and escheats to the State. The universe of what can come from estimation should only be those that are under audit or in the VDA program. What is the percentage of the estimation from those revenues. Revenues from companies that are filing and escheating property cannot be counted in that percentage.

Senator Townsend said that he understands Mr. Rosen's point, however they have looked at this data in a few different ways. One way was to ask what percentage of the overall revenue was related to estimation, to put the percentage into context. The average was 20%. To Mr. Rosen's point, 80% of general ledger audits relate to estimation. They have looked at this data in a few different ways for different reasons and there is not going to be one definitive answer. There are valid reasons for looking at this in different ways.

Representative Speigelman asked what the range the percentage was over the six year period that Deputy Secretary Gregor was talking about.

Deputy Secretary Gregor said that the percentage was as low as 13% and as high as 33-35%.

Senator Townsend asked if Deputy Secretary Gregor thought that the 80-85% was pretty consistent.

Deputy Secretary Gregor said that in terms of the general ledger audits that closed, it was.

Senator Townsend asked if the changes over the years were more related to the amount of funds coming in from other sources. He clarified that the actual percentage of general ledger audits that relate to estimation does not actually change that much.

Deputy Secretary Gregor said that is correct.

Senator Townsend asked, in terms of equity, if FY 13 is an outlier and that they should not expect to see those levels again anytime soon.

Deputy Secretary Gregor said that it was an outlier

in terms of equity and general ledger. It was more of an industry-wide clean-up of the books. They received a lot of money in transfer agents that year. In a typical year this will not be the case.

Mr. Ratledge said there are direct effects of changing various rules, and there can be an induced number that is either positive or negative. It is not as simple as looking at the numbers that have occurred historically, since it also depends on the rules that are in place at the time.

Deputy Secretary Gregor said that he made that point earlier when he talked about the increase that occurred after their enforcement program was implemented.

Stan Stevenson, Delaware State Bar Association (DSBA), clarified that 80-85% of general ledger audit collections result from estimation. That is pretty consistent over the six year period. 20% of total Delaware unclaimed property collections comes from estimation. That percentage fluctuates from year to year based on the amounts of other funds received.

Deputy Secretary Gregor said that is correct.

Senator Gregory Lavelle said that he realized that the Task Force has extended past the dates originally set in SCR 59. He asked if the letter Senator Townsend sent to Speaker Schwartzkopf and President Pro Tempore Blevins requesting an extension for the Task Force kept them in good stead.

Senator Townsend said that it did. He is still committed to producing a report for General Assembly Leadership on the findings of the Task Force and to producing legislation for the General Assembly to act on in 2015.

Senator Townsend then asked for comments and edits from the Task Force members on the Draft Report, beginning with the "Task Force Findings" section.

Mr. Tuinstra addressed bullet point number six, "For the auditing process, the Delaware Department of Finance recently has developed a focus on the largest Delaware corporations that regularly fail to file unclaimed property reports." He objects to the phrasing "large Delaware corporations." Mr. Tuinstra suggested using the phrase "some of the largest Delaware

incorporated entities” instead.

Senator Townsend said he would use “entities” instead of “corporations.”

Secretary Thomas Cook, DOF, said that he was not sure this was a recent development on the part of DOF.

Senator Townsend said that he works in corporate litigation, and in that field when the phrase “Delaware corporation” is used it typically refers to companies incorporated in Delaware as opposed to companies with operations in Delaware.

Mr. Tuinstra said that in the general public that may have a different connotation.

Senator Townsend said that he concurred with changing the phrasing to “companies incorporated in Delaware.”

Representative Speigelman asked if the word “largest” should also be added to the phrase.

Secretary Cook said that DOF has been focused on compliance. DOF is not going to audit the mom and pop sub shops, but they have been focused on making sure that companies are complying with regulations.

Senator Townsend asked Secretary Cook if he objected to the word “recently” being used in this point. Previous meeting minutes indicate that DOF has, in the past couple of years, increased its compliance efforts with regard to larger companies incorporated in Delaware.

Secretary Cook said that through Secretary Bullock’s VDA program and increased outreach to companies, the State has increased some efforts to target companies who did not respond to outreach efforts and did not enroll in the VDA program. He concurs with the use of the word “recently.”

Mr. Ratledge asked if DOF tries to focus its efforts on sectors that may have greater amounts of abandoned property than others, such as the securities industry, as opposed to a random sampling.

Secretary Cook said DOF does try to focus on certain industries.

Mr. Tuinstra said that when Kelmar presented, they mentioned that some of their audits are not necessarily non-filers but are filers. They look for companies that have under filed as well. Mr. Tuinstra suggested adding this to the Task Force Findings. He believes this is an important distinction to make.

Senator Townsend said there are ongoing audits currently that are related to the accuracy of the company’s filing. However, because audits take multiple years, a recent focus could have been forged to focus primarily on non-filers and yet there still are ongoing audits relating to filers.

Mr. Tuinstra addressed bullet point number nine. Obviously Deputy Secretary Gregor’s updated percentage will be included, but Mr. Tuinstra said that it would also be good to clarify that percentage by also including that 80-85% is the average percentage of general ledger audits that use estimation.

Senator Townsend said that he has no objections to adding that.

Mr. Ratledge referred to bullet point number five that states, “In terms of expressing concerns about the auditing process, companies that are aware of their legal obligations yet still fail to file annual unclaimed property reports are in a less sympathetic position than those companies that file reports annually.” A report could be filed that deliberately underreports. There is no measure for the accuracy of those filings. Something else needs to be inserted into this statement that specifies that the report filed by a company must be correct.

Senator Townsend said that the sentiment that companies who are not filing are not deserving of sympathy was expressed by nearly all Task Force members in previous meetings. He is happy to make a change to this bullet point if members feel that identifying another step in this process is necessary. The initial steps can be either explained or the statement can be reworded so that there are no additional implications.

Mr. Stevenson said he would like the word “required” to be inserted before “annual unclaimed property report” because some companies do not have any unclaimed property and are therefore not required by the Delaware Code to file.

Senator Townsend asked if it would be worthwhile to ask companies who do not have any unclaimed property to remit to still file a \$0 return. He asked if there were any objections to that idea.

Representative Spiegelman said that this idea is currently a “best practice” for companies.

Mr. Stevenson said that he does not have any problem adding that requirement. It would make companies more cognizant of their filing obligations.

Representative Spiegelman said he would support this as long as it is not a burdensome requirement for the company.

Mr. Rosen said that at one of the first Task Force meetings he had suggested that one way to make this requirement easier for companies was to include it on their franchise or income tax return.

Secretary Cook said that he would not support adding this to a current tax form, but he said there is an online filing system for gross receipts. An online system for filing this type of return could be built as well. That would cut down on paperwork and processing.

Rick Geisenberger, Chief Deputy Secretary of State, said that there are more than 1.1 million legal entities in Delaware. That would be a lot of filings.

Senator Townsend said he would consider pursuing this issue in legislation in 2015. He asked Mr. Ratledge if he was suggesting that the word “accurately” be inserted in bullet point five.

Mr. Ratledge said that could be one solution. Something needs to be added to make sure that companies are required to file correctly.

Senator Townsend asked Mr. Ratledge to clarify if he meant that the “sympathy” would only be extended to those companies that file accurately.

Mr. Ratledge said no, that you could go after people who have already filed. Even if a \$0 return is filed it is not a safe harbor in the context that was mentioned.

Senator Townsend said that this is not an item that necessarily requires direct action. It is more expressing

the findings of the Task Force. He is pleased that there is so much agreement on this point, that there should only be sympathy to companies that have filed accurately.

Mr. Stevenson said that “in good faith” should be used instead of “accurately.”

Mr. Rosen said that he disagrees. The term “accurate” is ambiguous and it is difficult to define “accuracy.” If a return is off by \$1, then it is not accurate.

Senator Townsend asked if the words “in good faith” instead of “accurately” would be more palatable.

Mr. Rosen said he would leave this out altogether. There is already no statute of limitations if there is fraud. Nothing further is necessary.

Mr. Ratledge said that the phrase “less sympathetic” is also very imprecise. It is just as imprecise as “accurately.” Why take one out and not the other. This is not a precise statement any way you look at it.

Mr. Rosen suggested using “non-fraudulent” instead of “accurate.”

Mr. Ratledge said that the definition of “fraud” is a legal definition.

Mr. Rosen said that “accurate” means a return would have to be exact. “Non-fraudulent” would require fraud to be proven.

Mr. Tuinstra reminded the Task Force that this is not an operative section; this is the Task Force’s ideas. He believes that “in good faith” would be a good addition to this bullet point. “Accurate” is too technical a term, but “in good faith” would be a good substitute.

Mr. Rosen said that “in good faith” probably meant the same thing as “non-fraudulent”.

Secretary Cook said PIT returns can be checked against other filed forms, but there is nothing to check unclaimed property returns against. He supports using the term “in good faith.”

Representative Spiegelman suggested including something in the Draft Report that would relate to the pending court cases about unclaimed property.

Mr. Stevenson referred to bullet number ten, “A Task Force member who is a professional statistician found nothing methodologically incorrect about the estimation methodology used by Delaware’s largest contract auditor.” He said that it was interesting in that it referred to the findings of a Task Force member, rather than the findings of the Task Force as a group. He said he was not sure he was willing to agree with the statement that there was nothing methodologically incorrect with the estimation methodology.

Senator Townsend agreed with Mr. Stevenson that he also would not say that he personally had knowledge of the soundness of the methodology. That is why it was specifically worded to be the view of one Task Force member.

Mr. Ratledge said he would like to correct this bullet point; he is an economist, not a statistician.

Mr. Houghton said the issue of the accuracy of the estimation and extrapolation methodology is very much at the core of at least one pending piece of litigation in federal court. He recommends deleting this point because only one Task Force member was able to have this interaction with Kelmar and he does not think this should be at the core of the Task Force’s deliberations. Mr. Houghton does not think there is a consensus among Task Force members on this issue.

Senator Townsend said he did not see any reason to delete the statement. The Task Force heard time and time again over the past several months criticisms of Kelmar with no specificity whatsoever. There was a sense that they performed simple, ‘back of the napkin’ calculations in audits. According to Mr. Ratledge, this is not the case. One of the most technically skilled members of the Task Force went out independently and spoke with Kelmar statisticians directly about these exact issues for a significant length of time. He believes that it is unbalanced to not have any mention of this in the report when the minutes are replete with mentions of unsupported criticisms of Kelmar’s methodology.

Senator Lavelle said that economists have different points of view. Other economists may arrive at different conclusions. He is not sure how binding that sentence is.

Senator Townsend said that it is interesting how

highly paid specialists frequently reach conclusions that happen to align with their client’s interests. This Report is not binding in any way. He believes that this is an important point that should be kept in the Report, but it is not solely up to him to decide.

Mr. Houghton said that he does not question Mr. Ratledge’s inquiry into this aspect of the issue, but this could lead to the inference that the Task Force as a group believes that the Kelmar or SAS methodology in the broadest sense is an appropriate method of extrapolation and estimation. It all depends on how that methodology is applied to a particular case. If this statement was to be included in the Final Report, Mr. Houghton would like a phrase included after it that mentions that there are a number of members of the Task Force that do not necessarily subscribe to the estimation methodology being appropriate and that it all depends on how it is applied on a case-by-case basis.

Mr. Tuinstra said that he appreciates the work that Mr. Ratledge did, but the Task Force did hear from holders (although anonymously) and they said that they consider the auditors’ methodology to be aggressive. He asked if that view could also be included. Both sides could be presented equally.

Senator Townsend said that he is not opposed to that, but the work Mr. Ratledge did go far beyond the anonymous comments that were received.

Mr. Tuinstra said that the Task Force heard different things from different people and that both viewpoints should be represented.

Senator Townsend said that nothing concrete was ever presented to the Task Force that refuted the information that Mr. Ratledge presented, much to the Senator’s frustration. There were plenty of opportunities for other companies to speak about their experiences and they chose not to.

Mr. Tuinstra said that was exactly his point. Differing points of view were presented anonymously to Task Force members. They were not as pointed as having issues with the methodology, but companies did say that they found auditors to be “aggressive,” too much information is required, and the audits take too long to conduct. The statement about Mr. Ratledge’s findings should not be removed, but the other perspective (of

the holders) should be added.

Representative Bryon Short said that Mr. Ratledge's findings and the anonymous comments from holders were two completely different types of statements. One describes the structure of the practice and the other describes the feeling of an audit.

Thomas Collins, Delaware Bankers Association (DBA), questioned whether this should even be referred to as a finding by the Task Force.

Senator Townsend said that it could be a note about the feelings of the holders about the auditing process.

Mr. Collins suggested that it could be included as a footnote. The findings should include things that the Task Force has come to a consensus on. It is clear from this conversation that there is no consensus on this issue.

Representative Spiegelman said that the current wording says "a Task Force member." While he respects Mr. Ratledge's expertise, another Task Force member has clearly had a different finding. He said he does not think it is appropriate to talk about the individual findings of Task Force members in a group report.

Senator Townsend said that he agrees with Representative Spiegelman to a point, but that he still believes that not including Mr. Ratledge's findings is an insult to him and his expertise. This is not just about Mr. Ratledge, however. A lot of people spend a lot of time making anonymous and nonspecific statements. He believes that Mr. Ratledge's investigation supersedes these anonymous statements.

Senator Townsend said he respects Representative Spiegelman's comment that the report should not be too individualized with each Task Member having to contribute their specific point of view. It is possible to insert a sentence with the point of view of the holders. He pointed out that Mr. Ratledge was not at all involved in the writing of the Draft Report; the views in the Draft Report are Senator Townsend's.

Senator Lavelle said that he does not think that this is an attack on Mr. Ratledge. He believes that the statements from COST from the holders' perspective are specific and are not vague at all. He understands

why these companies are uncomfortable with openly criticizing the audit system and why they prefer to remain anonymous. He believes that an extra sentence is needed for the perspective of the holder but that the Task Force should move on to the recommendations section.

Senator Townsend asked if the Task Force members had strong feelings about whether the holders' perspective should be added to the same bullet point as Mr. Ratledge's findings or whether they should be kept separate.

Leonard Togman, public, retired attorney at Potter Anderson, suggested stating that "despite the view of this Task Force member, other Task Force members disagreed," or that "it did not reflect the views of all members."

Senator Townsend said that he disagrees with Senator Lavelle that the statements made by holders are specific; he found the anonymous comments to be extremely vague with no details about specific instances and circumstances given. He asked if Task Force members would prefer he add another sentence to the current bullet point to reflect this additional viewpoint or add a sentence to indicate that some members did not agree with Mr. Ratledge's findings.

Representative Short said that he thinks that the two statements should be disconnected because they are two very different statements.

Senator Lavelle said that he has talked to state tax directors of very large companies in Delaware and they are frustrated with the Delaware unclaimed property program. There can be a sound methodology that is aggressive and a sound methodology that is not aggressive. No one is questioning the methodology, but they are questioning the aggressiveness of the auditing companies.

Secretary Cook said that the problem is no one had every defined what "aggressive" is. It is DOF's job to collect the unclaimed property due to the State.

Senator Lavelle asked if someone requested DOF's records from 1985, could they be found.

Secretary Cook said that DOF has an archive.

Senator Townsend still finds that situation ironic. He said that Mr. Ratledge investigated methodology, not the actions of the auditing companies. No one has ever approached Senator Townsend to say that the methodology in particular of these companies is questionable. Whether or not the auditors are aggressive is another issue. Senator Townsend said that if this particular point is going to continue to cause so much rancor he would be happy to rewrite it.

Senator Lavelle said he would like to thank Senator Townsend for the fantastic work he has done on this Task Force, which was above and beyond the call of duty. This is not an attack on Senator Townsend or Mr. Ratledge. The other members would simply like an acknowledgement in the findings that there is frustration on the part of the holders (as articulated by COST).

Representative Short asked if this discussion should really be focused on bullet point number three, "Although changes have been made in recent years that have helped to address the concerns of Delaware corporations with various aspects of the unclaimed property auditing process, several concerns remain. These include, among others, the length of the "look-back" period in the auditing process, the dominance of one audit firm in Delaware's audit portfolio, and the lack of a 'best-practices' manual for Delaware contract auditors."

Senator Townsend said that he did not mean to indicate that he is taking this personally. There is currently nothing in the Draft Report that indicates that the unclaimed property program is doing anything right, and he thinks that is a disservice to them. Part of the spirit of bullet point number 5 was to provide some of that balance, to show that there is sound methodology being used, as determined by a professional econometrician's preliminary review.

Mr. Houghton said that it would be helpful that if any Task Force members have suggestions for changes to the Draft Report that they also offer sample language for that change. He has known Mr. Ratledge for a long time and has a lot of respect for him and what he has accomplished. If this language is going to stay in the report, Mr. Houghton believes that Mr. Ratledge's name and title at the University of Delaware should also be used to give credence to the statement.

Senator Townsend asked Mr. Ratledge if he has any objections to his name being used in the Final Report.

Mr. Ratledge said he has no objections. The lack of specificity in the presentations was what drove him to contact Kelmar and do his own research into their methodology. Even the COST presentation had no direct information; it was all third-party stories. Real people need to come in with specifics.

Mr. Tuinstra referenced the packet COST distributed after their presentation. In one section, there is a list of specific issues that COST members stated that they found to be "aggressive."

Mr. Ratledge said that most of the things listed in that packet were issues of law, not methodology.

Senator Townsend said that he wanted to confirm that Mr. Ratledge did not mind being named in the Final Report and that no one on the Task Force minded him being named, that the points on the opposing viewpoints should be in two separate paragraphs, and the second bullet point would state that the Task Force has heard from Delaware incorporated entities that have concern about the estimation process.

Secretary Cook suggested inserting that these are COST-represented Delaware incorporated entities.

The Task Force members agreed on all counts.

Michael Barlow, Chief of Staff, Office of the Governor, has two recommendations. He first referred to bullet point eleven, "Notwithstanding active outreach by the Delaware Department of State, relatively few corporations accepted the opportunity to enter the Department of State's Voluntary disclosure Agreement program. The deadline for entry into that program has passed, and there is an open question whether another similar program should be developed." Mr. Barlow suggested clarification: relatively few as compared to what. If few companies joined then why would the Task Force consider extending the program. "Relatively few" should be quantified. The Administration considers it a success, with several hundred companies joining.

Secretary Jeff Bullock, Department of State (DOS), suggested emphasizing the large number who did not join. It begs the question of why 2/3 of the other

corporations did not join.

Mr. Barlow suggests using the facts and including the number of companies who did and did not join the program.

Representative Spiegelman suggested writing “enough companies responded that the Task Force considered it a success, indicating that the program should be continued.”

Mr. Ratledge thinks that using the exact numbers would be more helpful.

Alison Iavana, DOS, said that over 700 companies are enrolled in the program. One-third of the companies that received letters inviting them to join the VDA program did join. Other companies that did not get letters did enroll in the program.

Senator Townsend said that the fact that one-third of the companies that were invited joined the VDA program and two-thirds did not is a separate idea from the overall success of the program.

Mr. Houghton agreed that the numbers should be included and that the two ideas should be stated separately.

Senator Townsend agreed with Mr. Houghton. With regard to Representative Spiegelman’s point, the Task Force should consider the effects that this report will have on any possible renewal of the VDA program. Sen. Townsend is looking for guidance on where this statement should be included.

Representative Spiegelman suggested adding something to the bullet point that focuses on the success of getting one-third of the companies contacted to participate. It shows that there is interest in continuing the program.

Mr. Barlow referenced bullet point number eight, “Pursuant to current Delaware law, the Delaware Secretary of Finance makes the final determination of a party’s administrative appeal from the Department’s audit findings.” He said that mention should be made of the hearing officer who makes a determination before it is sent to the Secretary of Finance for final determination.

Representative Spiegelman asked if the hearing officer is employed under the Secretary of Finance.

Mr. Barlow said the hearing officer is independent, but is contracted by DOF.

Senator Townsend said he understands the concerns about this issue and would be open to clarifying the appeals process in the report. The appeal can be taken to the Court of Chancery after the Secretary of Finance makes a determination. Clearly people are concerned about the in-house nature of the appeals process, although this is not a unique situation.

Mr. Barlow said that he was concerned about the lack of specificity on this issue currently in the draft report.

Mr. Houghton said that the wording could be fixed by adding “although there is an independent reviewer who determines appeals in the first instance” before talking about the Secretary of Finance’s role.

Senator Townsend suggested writing that the Secretary of Finance’s determination follows a hearing process and can then be followed by an appeal to the Court of Chancery.

Secretary Cook referred to bullet point number twelve, “There may be opportunities to bring more of the auditing process in-house in order to achieve cost-savings for Delaware taxpayers, most specifically with the development of a VDA program.” He reminded the Task Force that DOF has always had a VDA program, and that DOS has only recently begun to run its own VDA program. This should probably be clarified.

Senator Townsend agreed with Secretary Cook. He then directed the Task Force to begin discussing the next section of the Draft Report, the “Task Force Recommendations.”

Mr. Tuinstra addressed bullet point number one, “The Delaware Department of Finance should develop a ‘best practices’ manual, and update its regulations accordingly, to ensure greater transparency and predictability as to what should be expected by holders during a Delaware unclaimed property audit. The Department should also ensure its contract auditors comply with this manual, and should publish this

manual prominently on the Department of Finance's webpages related to unclaimed property." Mr. Tuinstra asked for clarification on the audit manual name.

Senator Townsend said that he called it a "best practices" manual just based on the discussions from previous meetings. The title of it is open for discussion.

Mr. Tuinstra said that "best practices" manual has the connotation that the manual is a nice idea but that auditors are not required to follow it. Calling it an audit manual or audit regulations would indicate more strongly to auditors that they should follow it.

Senator Townsend said that he was not sure "regulations" was the best term. It had seemed in previous discussions that holders had wanted more transparency about the audit process. This would be a manual that companies should have access to so that they know what to expect during the audit and that auditors would have to follow.

Mr. Tuinstra said that it is a spectrum. An audit manual would just list the obligations of auditors. The Task Force could also require the creation of something that would include regulations where the rules for an audit are laid out. He feels that "best practices" is less effective than "audit manual."

Senator Townsend said it would be difficult to get a consensus on regulations from the Task Force during the last meeting, but asked what the wording should be.

Mr. Rosen suggested that "best practices" be put in quotations and that "policy and procedures manual" also be added.

Senator Townsend reminded the Task Force members that this is an ongoing, organic process. No matter how tightly these recommendations are written, there will be follow-up.

Mr. Tuinstra asked if the Task Force should be recommending how the manual should come about and what DOF should do to create it. Perhaps the recommendation should be more specific.

Senator Townsend said that there is a fair expectation that these recommendations will be addressed fairly quickly, within 2015 calendar year.

Mr. Tuinstra said that should be added to the recommendation. He then asked how the process of creating the manual would work, whether it would be a closed process or if outside input from stakeholders would be welcomed.

Mr. Togman asked if there would be a period for comments on the manual.

Senator Townsend said that for regulations there would be. In theory, this manual would not be a part of that. He would recommend that this manual be treated as if it was a regulatory document, but that it would not be subject to the entire regulatory framework.

Mr. Houghton said that this manual should be more than just an internally developed set of recommendations and proposals that are then published for comments. The best way to do this would be to try to have a collaborative process, where reasonable requests coming from the holders could be integrated into the new audit processes and procedures. If the holder community overreaches, this initiative will not work. There needs to be a balance between the two sides. The Division of Revenue may also want certain areas strengthened to help them perform audits. The gold standard is statute, but he does not think they have a place in audit guidelines. A working group put together by the Division of Revenue that includes appropriate stakeholders from the holder community would be ideal.

Senator Townsend said that he has some concerns about the term "working group" because those types of groups would be subject to various kinds of regulations. He is a full advocate for transparency in government, but he is not sure that the Task Force is looking, for example, for the level of formality that comes along with having a "working group" that is subject to FOIA and open-meeting notices and timetables. He noted that Michelle and Kiki are excellent at making sure that this Task Force complies with FOIA rules. Ultimately, this document would be publically available. The more formality that is involved in this endeavor, the less flexibility and time there is, and the more administrative requirements there are. It is a trade-off.

Secretary Cook said that DOF is committed to working on this. It benefits DOF as well as the holder community to have the audit guidelines clearly stated. This process could get dragged down with too many

formalities, which could keep them from creating the document they really would like to. Secretary Cook also questioned whether the companies who are being audited should be allowed to set the rules for the audit process. That is certainly not done in the personal income tax business. He would like their input, but he does not think that regulations need to be involved. He has no problem making this process as transparent as possible so that holder input is included.

Senator Townsend said that is an important point.

Mr. Ratledge said that many audit companies work in multiple states. If Delaware changes its regulations and processes too much, that will require them to change their internal structure. It may be very difficult to bid on a state that is too individualized.

Senator Townsend said that the Task Force as a whole has been interested in seeing more variety in auditing companies. Perhaps one way to achieve that would be to work with companies who do specialize in Delaware regulations. He is not sure if the regulations in this manual would be so significantly different than other states that it would require a change in audit company structure.

Mr. Ratledge said that some of the procedures from some of the companies are different and they have different business lines. If the procedures become much more rigid and only applicable to Delaware, this could be a problem.

Senator Townsend asked how this bullet point should be worded to balance the appropriate level of specificity and formality.

Mr. Houghton said there needs to be something included in this point that says that DOF must work with input from the holder community. Some states, like Michigan, have adopted very detailed policies regarding audit policies. There does need to be recognition in text that there will be an openness and access for the holder community to comment and give suggestions. It does not mean that all suggestions will be taken by DOF. It should also be stated that there is an expectation that this manual will be completed by the end of calendar year 2015 and that the process will be consultative and receive input from the appropriate stakeholders.

Senator Townsend asked if it would be possible for this manual to be completed by the end of the second quarter of 2015. He asked Secretary Cook how long it would take to create this manual.

Secretary Cook responded that DOF will start working on this manual immediately. It will be completed as quickly as possible. He thinks that the end of calendar year 2015 is an appropriate deadline.

Senator Townsend reminded the Task Force that these recommendations have no force of law.

Secretary Bullock suggested including in this bullet point people who do not have a financial interest in this area.

Representative Spiegelman said that finding people who do not have a vested interest but are still knowledgeable about the subject would be very difficult.

Secretary Bullock said that there are people currently on the Task Force who were not initially knowledgeable about the subject, and they seem to have picked it up very quickly.

Senator Townsend said there are other avenues to find people. He doubts that the conclusion of the Task Force will be the end of the communication between stakeholders in this industry. He does not think that each bullet point requires this type of specificity. He trusts that DOF will comply in good faith with the intentions of this report without so much formality in the report. All legislators on the Task Force will always be available to consult if the community does not think this process is going well.

Mr. Houghton said he thinks that if “appropriate stakeholders and interested parties” is included that Secretary Bullock’s concerns would be addressed. If there are other constituencies who want to comment, they will surely surface. He is not sure who they are, but if there are people who want to play in the arcane sandbox that is this business they will most likely make themselves known.

Senator Townsend confirmed that he would add that the manual should be completed by the end of calendar year 2015 and that it should be called an “auditing procedural guidelines” manual.

There were no objections from the Task Force members.

Secretary Cook addressed bullet point number two, “The Delaware General Assembly should modify the appeals process outlined in the Delaware Code so as to provide a more central role for third-party review, including replacing the Secretary of Finance as the final decision-maker in the administrative appeals process.” He said that DOF does an RFP to find a contractor. There are two companies that have responded, and one company had to disqualify itself because of a conflict. Secretary Cook chooses an arbitrator who reviews the case. Secretary Cook accepts, rejects, or modifies their recommendation. He has no problem being taken out of the accepting, rejecting, or modifying aspect of the situation. He believes that DOF should still be responsible for the selection of the arbiter.

Mr. Houghton asked if Secretary Cook would be open to not being the party that selects the reviewer. There could be a standing panel that Secretary Cook appoints who selects the reviewer. Each person on the panel can select who the reviewer should be. If there is deadlock, then someone like the President Judge of Superior Court can choose the arbiter. They could have statutory authority. The appellate process would include the Court of Chancery and the Delaware Supreme Court. He asked if there were any objections from the Task Force members to a process that would run like he described.

Mr. Ratledge said the problem that he has with the system is that the Findings section states that the Secretary of Finance and DOF would be responsible overall for this entire program. If people who are not affiliated with DOF are included then who would be responsible for the overall findings.

Mr. Houghton said the independent reviewer would issue findings just like they currently do. That would be the record of the case that gets presented if there are further appeals. The only thing the Secretary of Finance currently does is set up the process of selecting an arbiter and accepts, rejects, or modifies the arbiter’s report. The Division of Revenue does everything else.

Mr. Ratledge asked who would be an independent reviewer/arbiter in this circumstance.

Mr. Houghton said this is currently in the statute.

Mr. Barlow said that they are attorneys. Bill Quillen was originally supposed to be an arbiter but he ended up not being able to do it because of a conflict.

Mr. Houghton said that there are not very many people who would step up to do this job. He asked Secretary Cook if he got a lot of responses to his RFP.

Secretary Cook answered that he had not gotten a lot of responses.

Mr. Houghton said that the Task Force should consider whether they should change the necessary qualifications for an independent reviewer. Lots of members of the judiciary rule on matters that they are not expressly experts in. Since there have not been a lot of responses to Secretary Cook’s RFP it might make sense to develop a panel to select an arbiter. Retired lawyers could be a good source of these arbiters.

Mr. Barlow said that arbitration panels are typical in lieu of litigation. He asked if Mr. Houghton was recommending an arbitration panel in addition to litigation.

Mr. Houghton said yes. The only addition would be the panel, which would change who selects the arbiter.

Secretary Cook said that there have been four RFPs and one person has disqualified himself. DOF has tried to find more arbiters. He asked what the real concern was about this issue and if the concern was that there would be favoritism on the part of the Secretary of Finance.

Senator Townsend said that in the minutes of previous meetings when this was discussed, the concern was that entities would not even try to pursue an appeal because they feel that the deck is already stacked against them since the Secretary of Finance is the final decision-maker. The Task Force had suggested removing the Secretary of Finance as the final decision-maker. He is not sure if this would cause litigation to be avoided, but it could make the process more palatable for everyone.

Secretary Cook said he has no problem being removed out of the end of the process. However, this process is done all the time in state government.

Mr. Barlow said that when this was discussed at a previous meeting it was about the concept of an administrative law judge. They are typically hired by the department to which they report. Mr. Houghton's suggestion is a different approach, which would be that the two parties agree to a proceeding before an arbiter and would only pursue the case at a higher court if the arbiter oversteps their bounds. It seems as though everyone is comfortable with the Court of Chancery and its handling of these types of cases. It strikes him that creating an additional bureaucratic structure that is usually in lieu of litigation as a precedent of getting to the Court of Chancery is duplicative.

Senator Townsend said there could also be a system where an arbiter is used and the Secretary of Finance is removed from making the final decision; the case would go directly to the Court of Chancery. This would address the concern of entities that the deck is stacked against them from the get-go, but would not solve the issue of the difficulty in finding someone to act as an arbiter. He would suggest that the Task Force recommend that there is a change to the program that could be followed up with legislation in 2015.

Mr. Togman said that Judge Richard R. Cooch of Delaware Superior Court has just put out a request for a panel of commissioners or hearing officers for condemnation cases. He was solicited for this panel. In the past there has always been a bench of people available for these cases, but there is not anymore. This was sent out for retired lawyers for volunteers. Each side in a case will get the list of available volunteers and be able to pick who they would like on the panel. This could be adapted to fit Mr. Houghton's suggestion of a panel.

Senator Townsend said that this is an important point. This should be something that is followed up on in 2015.

Senator Townsend addressed bullet point number four, "The Delaware General Assembly should revisit the issue of instituting a 'cooling off' period before State employees involved with the State's unclaimed property program are permitted to accept employment with one of the State's contract auditors." He asked if there were any edits from the members.

Secretary Cook asked if this referred to all State

employees, not just Department of Finance employees and includes people who do not work directly with contract auditors.

Senator Townsend emphasized that this Report is not a statute. He said 'yes' to Secretary Cook's question. An adverb could be added to the statement to qualify the extent of the person's involvement. This bullet point does state that the General Assembly should "revisit" the issue.

Mr. Togman said that it is not unusual for contracts with independent contractors to say that they will not hire former State employees for a particular amount of time.

Mr. Houghton said he was not sure exactly what "revisit" meant in this context. He was not aware that the General Assembly had discussed the issue.

Senator Townsend said that legislation had been filed prior to this Task Force but that was not pursued.

Mr. Houghton said that there had been two senior staff members who had worked for the Division of Revenue who left to work for Kelmar. He does not know if having secretarial staff leave to work for Kelmar should fall under this category or if maybe a materiality standard should be put into legislation.

Senator Townsend suggested writing "State employees involving senior positions."

Mr. Houghton said he thought that would work.

Mr. Barlow said that it has been difficult to find people who do not have a vested interest and who are knowledgeable about this situation. For people who do this work for a living, there are few places to go. Another thing that was discussed during the task force was having the State do some auditing work in-house. A too strict cooling-off period would handicap that effort. Having the legislature revisit the issue would be a good way to handle this. The State could have to pay people a lot more money to make it worth their while to step out of the industry during this cooling-off period.

Senator Lavelle asked if there are already regulations in place that prohibit Cabinet Secretaries from leaving their positions and immediately becoming lobbyists. He

asked if that could simply be extended.

Mr. Barlow said there is currently a two-year limitation for working on something that a person had a material role in while in State employ.

Mr. Houghton said the former Audit Manager for the State left the Division of Revenue to work for Kelmar immediately after. He is not working on Delaware-related work. Don't people think that is a problem.

Senator Townsend said that it could be a problem and as such the Task Force would like the General Assembly to revisit the issue, potentially only having a cooling-off period for senior staff members.

Senator Townsend referred to bullet point number five, "The Delaware General Assembly should amend the statute of limitations relating to unclaimed property audits so as to avoid the outcome in which annually-filing holders are audited only after the passage of time beyond reasonable record retention requirements. The General Assembly should make additional modifications to the statute of limitations so as to confirm that, for annually-filing holders, investigations of fraud prior to commencement of a fraud-based audit should be limited to the past 6 years of filed reports." He is not sure the language in this bullet point says what the Task Force meant on this issue.

Mr. Stevenson said that he believes that the look-back causes more stress in the holder community than the statute of limitations does. People are being audited for filed returns after the three- or six-year period has expired on the theory that there is a chance that fraud exists.

Senator Townsend asked how you could possibly get away from that. If there is fraud then no statute of limitations applies. In order to find fraud, you have to look at the past filings.

Mr. Stevenson said that no one opens up an audit hoping to find fraud. Fraud is found during the course of an audit. If fraud is found, then the period of review is extended backwards.

Senator Townsend said that the law could be changed. The Secretary of Finance could be asked if this actually occurs in practice.

Mr. Tuinstra said there is no point in having a statute of limitations if every audit is thought to have fraud and is extended back twenty years. The statute of limitations has to actually mean something.

Senator Townsend clarified that they were referring to companies that have filed reports. In theory, they are no longer the focus of audits anyway. He asked Mr. Tuinstra to be more precise with his comments.

Mr. Tuinstra said you can either start out with the assumption that fraud is present and do a look-back of twenty years to see if it is in fact present or the statute of limitations (three or six years) can be looked at first for fraud or underpayment and then if it is present then years further back can be looked at. They are hearing that Kelmar is going back and initially asking for twenty years.

Senator Townsend asked if he was referring to filers or non-filers.

Mr. Tuinstra said that Kelmar was auditing filers and non-filers. The question becomes what happens to the statute of limitations.

Senator Townsend asked if these complaints were coming from companies that were non-filers. It is an important distinction. He asked if the Task Force thought that there should be different statutes of limitations for filers and non-filers. If there is fraud present, the statute of limitations does not apply. It sounds like members are hoping that auditors go first to the years that were filed and identifying the accuracy of those reports before they randomly pick a year to see if it is also accurate. Has there actually been actual evidence that this has occurred. This could be something that is included in the manual.

Mr. Tuinstra said that the testimony from companies that COST provided showed that 100% of the companies who responded to their survey and were under audit were filers and there was a look-back to 1986. He does not believe these are hypothetical cases.

Secretary Cook reiterated that he has said repeatedly that for the last few years, DOF has been focusing their audits on companies that have not responded to Secretary Bullock's invitation to join the DOS VDA program. It will take DOF many years to get through

that population of companies.

Mr. Tuinstra said that has only been a development in the last couple of years. The way that the statute of limitations should be applied should be very clear.

Senator Townsend said that this bullet point could be separated into two, since the first sentence is really a separate issue. He said Mr. Tuinstra's concerns relate more to the second sentence of the bullet point. He does not think the Task Force heard about any specific problems with the application of the statute of limitations; the concerns being expressed now are more about hypothetical issues with the statute of limitations, of fishing expeditions. He is not sure how to address this hypothetical issue. He suggested adding to the report, "statutorily prohibiting DOF from doing an examination of earlier years until the first six years are found to have indicia of fraud."

The Task Force members agreed.

Secretary Bullock asked that before the Task Force adopts this recommendation if someone could bring up a real example of this type of situation occurring.

Senator Lavelle said there might not be an example. You're not supposed to commence an audit on years that are closed if no fraud is found in the most recent 3 – 6 years. If this is already prohibited, what is the harm of adopting this recommendation. No harm, no foul.

Michelle Whitaker, DOF Audit Manager, said that the examination look-back is not based on the statute of limitations. The statute of limitations is not the limit of review. The statute of limitations limits DOF's ability to collect based off of filing history. They can review historical information. Her concern would be if the period of review is limited by the statute of limitations that holders will file for three or six years, stop filing, and then they are off the radar. She is concerned about inconsistent filers. The statute of limitations limits DOF's ability to collect, not their ability to review.

Mr. Tuinstra said that non-filers have no statute of limitations.

Senator Townsend said that the holder community is asking the Task Force to put somewhat of a lockdown on DOF. They do not want to go through audits that

go 15 – 20 years back when there are no indicia of fraud. He can understand that. Senator Townsend also understands DOF's point. He is considering changing the language to "The General Assembly should consider the possibility of" and then cleaning up the language in the recommendations based on the conversations in this meeting.

The Task Force did not object to this.

Senator Townsend referred to the first sentence of the bullet point. He said that Delaware does not actually have a statutory time period beyond which books and records can be disposed of. There's no statutory requirement or prohibition. It sounds like there is no way to solve this issue that companies destroy their records and then are later audited and have no proof of unclaimed property. He proposes the first sentence of the paragraph is deleted since it cannot be solved.

The Task Force did not object to this.

Senator Townsend referred to bullet point number six, "The Delaware Department of Finance should undertake efforts to renegotiate downward the length of its current contracts with unclaimed property auditors so that no contract with said auditors is for a longer time period than [XX] years per initial or renewed term."

Secretary Cook said that the assumption is that DOF is not going to renegotiate with contract auditors and it is going to cost the State more money. DOF has lengthy contracts with contract auditors in order to lock the price in at a lower level. If the contracts are shorter in length, there is a possibility that the price will be higher when the contract is renegotiated.

Representative Spiegelman said there is also a possibility that a market will be created by which increased competition will drive prices lower.

Senator Townsend said he did not recall hearing at previous meetings that the longer contracts could help keep the prices lower and save taxpayers money. These contracts do not guarantee any level of income for the contract auditors. They guarantee a relationship with the State. There are multiple agreements with various auditors; the State is not required to assign any particular auditor a certain percentage of the work. This is now becoming like four-dimensional Vulcan

chess. The maximum number of years for contracts was deliberately left blank in the Draft Report.

Senator Lavelle said that he thinks that with increased competition and developments in technology that there should be better prices available.

Secretary Cook said that this is a limited universe. DOF has reached out to try to bring in qualified auditors, but there are not that many available. He does not think that the Task Force wants DOF to renegotiate contracts so that the State is paying more.

Senator Lavelle said of course not. If the contract auditor is in the middle of an audit there is no point in pulling it from them and starting over with another contract auditor.

Senator Townsend said that the current contract with Kelmar expires in 2019 and was a nine-year contract with a five-year extension. He asked if Kelmar had said when the contract was being negotiated that if Delaware did this 9 + 5 year contract with them that they would give them a better rate.

Ms. Whitaker said that was not necessarily a part of the negotiation, but that is the reality. If the State negotiates more frequently, their costs could go up.

Mr. Houghton said that the State's costs could also go down. He understands that the State does not want to be in the position that Kelmar threatens to raise their rates if the State does not enter into a certain length of contract. However, Kelmar has made \$200 million from Delaware. Delaware does have a significant amount of leverage in this situation. He said there is no other precedent in Delaware for the State having such a lengthy contract with a contractor.

Ms. Whitaker said there are not many contractors available that can provide the quality level of work that the State's current contract auditors do. It is a limited pool. DOF would welcome new contractors.

Mr. Houghton asked if DOF would give them the opportunity to work for the State if they would only sign a short contract.

Deputy Secretary Gregor said that it has nothing to do with the length of the contract. DOF is currently

adding new contractors.

Senator Townsend said that he heard at previous meetings that there is a sense that there are contract auditors who are not staffing up because they are not sure if they are going to get Delaware business. DOF is not going to take a chance on disrupting the unclaimed property revenue stream for the State by shifting their work to a small company who has not proved that it can handle the same amount of work that Kelmar can.

Mr. Rosen said that it looks better if it is a five-year contract; it is partly perception. If Kelmar is so good and so capable then it is likely that the contract is going to get renewed anyway. The State could want to renegotiate or terminate the contract for some reason.

Senator Townsend said that the contracts do not lock the State into a particular distribution of labor; the State can divvy up the work however it thinks best among different auditors. He agrees with Mr. Rosen's point.

Secretary Cook said he would be fine with the contract limit being five years. He is still going to try to get the best deal for the State.

Senator Townsend said that there could be any number of renewals after the initial period. This would be structured to give the State more flexibility, however he reminded the Task Force that this Report constitutes recommendations, not a binding statute. The Task Force agreed to a five- year limit for contracts.

Mr. Barlow said that the current language of this recommendation applies to the current contracts DOF has with contract auditors.

Senator Townsend suggested adding another sentence to say that the same recommendation would also apply to future contracts.

Mr. Houghton said that the State should be able to renegotiate the fees before the end of their contract. This is not an uncommon practice for a client that has provided a significant amount of business for a contractor.

Mr. Stevenson agreed with Mr. Houghton. The State is in a good negotiating position.

Senator Townsend said that is possible, but this is a delicate dance since Kelmar is a very highly qualified contract auditor.

Senator Townsend referred to bullet point number seven, “The Delaware Department of Finance should undertake efforts to achieve more balance among the contract auditors who provide services to its unclaimed property program. The Department should provide an annual update of this balance to members of the Delaware General Assembly.” He asked if the Task Force had any comments to make about this bullet point.

Senator Lavelle asked how DOF currently does this.

Secretary Cook explained that as DOF starts to send out new audit letters, DOF tries to redistribute auditing work. Some contract auditors have specialties in certain areas. DOF is actively trying to bring in more contract auditors.

Senator Townsend said that diversifying the contract auditors’ portfolio comes at the expense of losing some very qualified contract auditing companies. In theory, diversifying seems like a good idea, but it is more complicated than that.

The Task Force had no specific changes to make to bullet point number seven.

Senator Townsend moved to bullet point number eight, “The Delaware Department of Finance should continue its efforts to enhance the reunification process for owners of unclaimed property, including the use of online options and more secure forms of reunification for higher-value property. The Department should provide an update regarding these efforts to members of the Delaware General Assembly.”

Secretary Cook said that this is something that DOF is in the process of doing.

Senator Townsend said that he and other members of the Task Force were struck by the dividends system.

Secretary Cook said that DOF has instituted a new system. They are concentrating specifically on the dividends issue and are making sure that claimants receive the dividends as well.

Senator Townsend said that he would like the dividends being returned without the person having to file a request for them to be included as part of the policies and procedures.

Deputy Secretary Gregor said that is the current plan. DOF is working on returning shares before the dividends.

Senator Townsend referred to bullet point number nine, “The Delaware Department of Finance and Department of State should enhance their efforts to bring audit and VDA processes in-house, so as to ensure efficient expenditures of Delaware taxpayer funds and minimize expenditures on higher-cost contractors. The Department should also increase staffing levels as needed to achieve any of the other recommendations included in this Report.” He asked if there were any questions or concerns. He said this bullet point would be dependent on what the future VDA program looks like.

The Task Force had no objections to this bullet point.

Senator Townsend referred to bullet point number three, “The Delaware General Assembly should amend the Delaware Code to adjust the ‘look-back’ period in Delaware unclaimed property audits, create a new VDA program in consultation with the Departments of Finance and State, and ensure the look-back periods in any ongoing VDA processes achieves an effective balance of incentives inherent in the two types of programs (audit and VDA).”

Secretary Cook said that any changes to the look-back period will have a financial implication for the State revenue. There is a balance that needs to be struck.

Mr. Togman asked if DOF has estimated figures for what the reduction in revenue would be if the look-back was moved to different years.

Deputy Secretary Gregor said that the data he has is in terms of general ledger audits. It does not account for the fact that there may be a reduction in compliance. Currently the look-back is at 1986. If the look-back was moved to 1991 there would be approximately a 15% loss in general ledger collections, which would amount to \$15 million. If the look-back was moved to 1996 there

would be approximately a 40% reduction in revenue, and if it was moved to 2001 there would be about an 80% reduction. This is a policy issue that has to be considered.

Mr. Houghton said that this is an area where the Task Force needs to be specific and embed this in legislation. It needs to be done sooner rather than later. The current look-back is at 1986, but there are audits currently underway that may not be finished by the time that expires in June, 2015 who will then have a 1981 look-back. This is dramatically out of kilter with the Uniform Unclaimed Property Act, where the look-back is closer to ten years. He believes that the Delaware look-back needs to be moved significantly forward. He believes the length of the look-back is a flashpoint for future litigation. It is an incentive to sue. Pending litigation has shown that judges have some concern about the way Delaware extrapolates and estimates back to 1981/1986. There has not been a ruling yet, but the look-back should be moved forward.

Mr. Houghton recommends moving the look-back forward to at least 1993 for all pending audits. The VDA look-back should be moved to 1996. A process should be put in place that does not have a stagnant look-back. It should be a rolling look-back period depending on the year that the audit commences. For example, if the audit commences in 2015, it would be a 20 year look-back which would be 1995. If the audit begins in 2016, the look-back would be to 1996. He noted that if a court determined that the entire process is invalid and that there is a constitutional problem, there may be a request for refunds.

Senator Townsend asked what year the look-back was formally put into statute or regulations.

Bob Byrd of The Byrd Group, LLC, said it began in 2001.

Senator Townsend said that might be a date that a court would find to be of some importance. He referenced Mr. Houghton's statement that if the look-back is ruled to be unconstitutional that holders would ask for a refund. He asked why a holder, who had recently gone through an audit, would wait for a court case before deciding to sue for a refund if they see the changes this Task Force is making.

Mr. Houghton replied that it is one thing for a State to change its policies and procedures. That is done all the time. That does not give companies a basis to seek a refund. However, if a court were to rule a process to be unconstitutional that would be a different issue. He thinks that the Task Force should recommend to move the look-back forward. He is not sure what the position of the Division of Revenue is on this.

Secretary Cook said that over the past several meetings of this Task Force, it has heard many times that DOF is focusing on auditing non-filers. The Task Force is not sympathetic to them. Secretary Cook asked why they should move the look-back forward. That would be rewarding them. His job is to collect revenue for the State of Delaware tax payers. He does not believe that moving the look-back forward would be fair to them. This issue should be addressed, and DOF has been working on doing that. He thinks that they should wait to see the results of those efforts before deciding to move the look-back period.

Senator Townsend said in his opinion, there should be language in the Report that provides guidance. It seems unlikely that there will be agreement on the year at this meeting. The fiscal implications need to be more thoroughly examined. Senator Townsend asked if it would be possible to do a hybrid system, where the look-back would be changed so that filers and non-filers have a different look-back. The statute of limitations does some of that already, but perhaps this would be a good addition.

Representative Spiegelman suggested having different systems for companies that have been audited already versus those that have not.

Senator Townsend said that companies who have already been audited are indemnified. The hope is that once a company is audited they will start complying and filing. Senator Townsend referenced Mr. Ratledge's comment from an earlier meeting, that Y2K had really changed the playing field. Companies are keeping much better records now that there is an increase in technology. A lot of the unclaimed property that is out there that is owed to the State is from the pre-Y2K period. That does seem to be reflected in the figures that Deputy Secretary Gregor presented. Senator Townsend can see companies waiting until the rolling look-back

passes and then being willing to be audited because there will be much less money to collect.

Mr. Houghton said if the State has a concern about that they can start aggressively auditing companies who will age out of the look-back. Many companies do not know that they owe any of this. They believe it is all estimated mumbo jumbo liability which is estimated using more current information constructing liability for periods for which neither the company nor the State of Delaware have any records. Companies cannot disprove an inference that has been created that an item from 2004 has an extrapolated effect and creates a liability for 1981. There needs to be specificity in this language or Mr. Houghton is afraid that nothing will happen.

Senator Townsend said that he does not think nothing will happen. Because of the time constraints of the Task Force, it may just be difficult to create that sort of specificity today.

Mr. Houghton asked how this would then be addressed. Would it be draft legislation and would the Task Force members have to lobby in Dover. How should they communicate that they strongly believe that the look-back should be changed. Are they supposed to negotiate with the Division of Revenue.

Senator Townsend said that he can only speak for himself, but he is committed to this process. This Task Force will most likely result in multiple bills. There will probably be a bill early in Session and a bill later in Session.

Representative Spiegelman asked why Mr. Houghton cannot both draft legislation and lobby and also work with the Division of Revenue.

Mr. Houghton said that they could, but it sounds like there is a major difference of opinion between State officials and members of other groups.

Senator Townsend asked Mr. Houghton what he meant when he asked how to approach the situation. Did he mean on a policy or procedural basis.

Mr. Houghton said both. This is one of the most important issues to be discussed by the Task Force.

Senator Townsend said that the language in this bullet point, "The Delaware General Assembly should amend the Delaware Code to adjust the 'look-back' period in Delaware," is pretty strong language relative to the history of this issue in Delaware. It would be irresponsible to try to come up with a definitive date for the look-back at this meeting. The fiscal implications need to be more closely considered.

Mr. Houghton said that he appreciates the goodwill and intentions of the members of the General Assembly sitting on this Task Force as well as the members of the Administration. He looks forward to future discussions on this issue.

Mr. Ratledge said that Mr. Houghton was representing the holders while Mr. Ratledge is representing the public. The money does not belong to the holders; someone else has property rights over the money. The Task Force needs to address this issue. He reminded the Task Force that the determination of the look-back is often a negotiation between the holder and the State, and the holders have a lot of input in the process. The rate is not recalculated. If the abandoned property amount is \$0 then the holder does not have to pay anything. Current bookkeeping is likely to be better than it was in the past, due to technology, and holders may actually prefer using more recent data. Holders have "the people's" money, and the Supreme Court has been very clear that it should be returned to them.

Mr. Tuinstra asked if something referring to a "rolling look-back" could be added to this bullet point.

Senator Townsend said that it could. He is not sure if the Task Force members all agree with that.

Mr. Houghton asked if the Task Force members could vote on the issue.

Senator Townsend said that given his understanding of the history of this issue, to have a public proceeding involved in this issue is pretty impressive. He intends to continue to have conversations about this issue to address this legislatively, but is concerned about the amount of specificity that some members are requesting for this Report.

Mr. Houghton asked Secretary Cook if the Administration opposes including a "rolling look-back"

in the Report if the look-back date is not moved forward.

Secretary Cook answered that because this has such a huge fiscal impact on the State, he would have to see the details of the proposal before he could make a determination.

Senator Townsend asked the members of the holder community present if the idea of a hybrid structure, in which non-filers do not get much relief, was palatable to them.

Mr. Houghton said that he thinks there would be a problem with that. Many companies have only heard about unclaimed property in the past couple of years as the issue has received more attention. Some companies have only started filing 3 – 6 years ago.

Senator Townsend said that Secretary Bullock sent out thousands of letters to companies notifying them of the DOS VDA program. This was a much more beneficial VDA program and most companies still chose not to join. This is an issue of fairness, as Mr. Ratledge eloquently mentioned earlier.

Mr. Houghton questioned whether this is in fact Delaware's or the public's money since the amount of money is being estimated and extrapolated for older records that do not exist with very recent records. Many companies would argue that it is not Delaware's money, that it is fictitious. He is concerned about nothing being done about this issue because in the previous unclaimed property task force (2006) the same issues were brought up and there was no action.

Senator Townsend said that he would not want any lack of action to be attributed to the current Administration, since they were not in office at that time. He does not want to make any judgments about the previous Administration because he was not present to witness it. It was his understanding that the previous Task Force Chair lost his reelection campaign before the recommendations could be enacted. Senator Townsend is glad that he broke that streak. He is pledging to remain committed to these issues and understands the concerns of the Task Force members.

Mr. Togman said that any change will impact State revenue. All members are Delaware residents and are mindful of that fact. He wants Secretary Cook to

know that they appreciate the work he has done, but the unfairness of the present law requires changes. He accepts Senator Townsend's pledge that there will be legislative action on this issue in 2015 and is willing to accept the language proposed. He appreciates Senator Townsend's action on this issue, as do the other Task Force members.

Mr. Stevenson said that he was originally concerned about a different process for filers and non-filers because non-filers could still be in compliance with the law. Companies are only required to file if they have something to remit. He would be more comfortable if the audits first look at the most recent six years to see if there are indicia of fraud before they can look farther back.

Senator Townsend said that if DOF is looking at records older than six years when there are no indicia of fraud, he would question their judgment. He does not think that is actually happening, but it might be. He is not sure how to craft a law that addresses this. If this is in fact happening, it should stop. This issue is, however, distinct from companies who have no statute of limitations because they have never filed. He is open to trying to draft a law that distinguishes between these two categories.

Secretary Cook said that audits are conducted until it becomes clear that there is no unclaimed property. The audit stops as soon as that determination is made. Secretary Bullock mentioned at an earlier meeting that the goal of the administration is to increase compliance. Secretary Cook is concerned that moving the date of the look-back will not increase compliance.

Mr. Barlow said that he agrees with Mr. Ratledge about the issue of fairness. There has been a huge amount of outreach to the corporate community over many years; ignorance at this point would be willful. Even if a company is actually ignorant of these laws, ignorance has never been an excuse for not obeying them. Compliance needs to be improved. This was mentioned in the resolution that created this Task Force. The rolling look-back does not do anything to increase compliance because it creates an incentive for companies who are sitting on abandoned property to continue to do so until the look-back period passes that date. That needs to be considered.

Secondly, the concept of a look-back date that is anything close to 1993 is fundamentally unjust. Companies joined the DOS VDA so that they could have a shorter look-back period. Making the look-back period shorter to everyone undermines that program and the companies that were trying to comply. That is a real unfairness.

Mr. Houghton said that there are at least two reasons why those discussions would not be as uncomfortable as one might think. He proposes that the look-back period for companies in the VDA, regardless of when they joined, be moved to 1996. The ability to process liability in the VDA is basically a managed audit. This is dramatically different than an audit done by a contract auditor. He believes this is defensible.

Secretary Bullock said that he is not sure that he has heard much talked about in the meeting today that will increase compliance. He does not have a problem with moderating the look-back period, but how it is done has to be done in a way that relates to the real world. This is a very complicated issue and this has to be dealt with in a way that does not cause other problems for the state.

Senator Townsend said that he is not convinced that the corporate community is even going to be pleased with the look-back changes they are proposing, but he could be wrong.

Mr. Tuinstra said that there is not a lot of sympathy for non-filers. The issue is that the look-back has not been adjusted in a long time. Moving it forward would take some pressure off of the State. There is a lot of buzz in the corporate community about how they should attack this issue from a litigation perspective.

Senator Lavelle said there is a dispute over whether the money being collected in revenue by the State belongs to the holder or the State. He asked the Administration what their opinion was on the possibility of litigation and an adverse ruling.

Secretary Cook said that DOF is monitoring these legal proceedings.

Senator Lavelle said that he heard that DOF posts ads in the newspaper notifying owners of their unclaimed property. He asked why DOF does not just send them a letter to notify them.

Deputy Secretary Gregor said that in securities they do send a letter. Moving forward, they are looking at using things like LexisNexis to assist with finding current addresses so that they can send letters for more types of unclaimed property. The other question is why the holders are not doing their own due diligence. They are supposed to, but it is not law and they sometimes do not.

Senator Townsend said that there are several DOF initiatives that are ongoing that work to help reunite owners with their property. They can follow up in 2015 with legislation on this issue as well. He also does not think that a court ruling would gut the program forever. It might create a quick and harsh outcome that the State might ultimately get to over the course of time anyway. A district court will not change the Supreme Court's ruling that the holder should not be able to keep unclaimed property. The way in which the program is administered may be changed by a court ruling.

Mr. Houghton said that Delaware does not have any statutory pre-remittance due diligence. Other states do. If Delaware chose to put that into law, he doubts the corporate community would oppose that.

Senator Townsend asked if the corporate community would oppose it because of the administrative burden it placed on them.

Mr. Houghton said no, he did not think they would object.

There was disagreement from DOF representatives.

Mr. Houghton said that the thing that holders really object to is the estimated and extrapolated general ledger audit money. He agreed with Senator Townsend that a district court is not going to overturn the priority rule set by the Supreme Court. However, the estimation and extrapolation methodology may be overturned. The Task Force has heard today that makes up 80 – 85% of general ledger audits. That is what could be lost.

Senator Townsend said that one has to wonder if that would only be lost to the extent that companies were not on notice for those years, as opposed to them being on notice for a certain period of time. That can be a meaningful distinction.

Mr. Stevenson said that another important consideration is that companies may decide against being incorporated in Delaware and may move to another state with a more favorable look-back period. Companies voluntarily choose to incorporate in Delaware. How Delaware decides to handle these issues may make them change their minds.

Mr. Barlow said that Mr. Stevenson's point is very important. Companies do have a choice in where they incorporate. Delaware has been trying to improve the corporate experience with the 2010 law creating an appeals process and the 2012 law creating the DOS VDA program. They have to do this with consideration that they have to be fair to other corporations who have complied with the law.

Secretary Bullock said that the State's focus on that balance has resulted in fewer complaints from the corporate community. Some companies have voluntarily

decided to not comply, and every member of the Task Force at one time has said that they should be shown no sympathy. Secretary Bullock thinks the Task Force should stick with that approach, which will help them avoid some of the chronic problems that have occurred in the past. Things are turning around now with recent initiatives from DOS and DOF.

#### PUBLIC COMMENT

There was no comment from the public.

Senator Townsend thanked the Task Force members for attending and for their comments. He will be circulating the Minutes from this meeting, the Minutes from the meeting on October 2, 2014, and the final Draft Report in the next couple of weeks. Senator Townsend looks forward to 2015 and continued conversations about this issue.

The Meeting was adjourned at 3:59 p.m.