State Law & State Taxation Corner

Should a State's Right to Claim Custody of Abandoned Property Dovetail with the Owner's Rights in that Property?

By John A. Biek

Introduction

Under state abandoned property laws, the state "steps into the shoes" of the apparent owner of an item of unclaimed property recorded on the books of the business "holder" and takes custody of that property item on behalf of the apparent owner. The state is asserting a derivative claim to the property item, so it stands to reason that the state's claim to the property item, pursuant to its abandoned property law, ought to be limited to whatever rights the apparent owner has in that property item *vis-á-vis* the holder. The state abandoned property law should not redefine the terms of the commercial transaction between the holder and the apparent owner so as to give the state *greater* rights in the property item than the apparent owner would be entitled to claim from the holder.

This theory is certainly consistent with the principles of state abandoned property laws, but it has not always proven to be the case. This column discusses several examples of states modifying the terms of the commercial transaction between the holder and the apparent owner in a way that gave the state a more extensive right in the property item than the owner would have been able to claim from the holder. Sometimes this resulted from the way that the state's abandoned property law was drafted, other times it stemmed from the state's administrative policy. However, state abandoned property administrators who do not keep the derivative claim principle in mind when asserting these claims risk overstepping the mark, as demonstrated by some of the cases discussed below.

General Principles of State Abandoned Property Laws

All 50 states and the District of Columbia have enacted abandoned property statutes that require a business (referred to as the "holder") to report and remit

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to the appropriate state the cash value of intangible personal property that (a) constitutes a debt or obligation owed by the holder, in the ordinary course of its business, to a payee such as a customer, vendor, employee or shareholder (referred to as the "apparent owner") and (b) has remained unclaimed by the apparent owner throughout the "statutory dormancy period" prescribed in the state's abandoned property statutes.[1] Many of these state abandoned property statutes are based on one or more of the three "uniform acts" that have been drafted by the National Law Commission (formerly known as the National Conference of Commissioners on Uniform State Laws).[2] All of the state abandoned property laws are now custodial in nature, meaning that the state's assertion of a claim to the property does not cut off the owner's rights to claim the property (which would be terminated under "escheat" laws). Rather, the state takes custody of the item of unclaimed property in perpetuity until the owner (or a holder that has reimbursed the owner) comes forward to present a claim to the state for payment of the property.[3]

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Under the priority rules established in the U.S. Supreme Court's decisions in *Texas v. New Jersey*[4] and *Delaware v. New York*,[5] the state of last known address of the apparent owner of the unclaimed property, as shown in the business records of the holder, has the first priority claim to the unclaimed property.[6] If the owner's state of last known address is unknown, or if that state does not have abandoned property laws that will apply to the property, then the holder's state of corporate domicile (generally, its state of incorporation) has the next best claim to the unclaimed property item.[7] Under the Uniform Acts, the "corporate domicile" of an unincorporated holder is the state where the holder's principal place of business is located.[8]

State abandoned property laws broadly define the types of unclaimed property that escheat to the state. The 1981 Uniform Act provides a typical list of examples of unclaimed property, which includes monies, checks, drafts, deposits, interest, dividends, credit balances, customer overpayments, gift certificates, security deposits, refunds, credit memos, unpaid wages, unused airline tickets, unidentified remittances, stocks and other intangible ownership interests in business associations, monies deposited to redeem or make distributions with respect to stocks, bonds, coupons and other securities, amounts due and payable under the terms of insurance policies, and amounts payable under employee retirement and other benefit plans.[9] The 1995 Uniform Act provides similar examples of "property" that escheats under its provisions.[10]

Even though these statutory definitions of abandoned property may be expansive, they are still subject to the fundamental principle that only *liquidated* (*i.e.*, fixed and with a definite value) liabilities of the holder may be presumed abandoned and reportable to the state. The 1995 Uniform Act defines the term "property" to mean a "*fixed and certain interest* in intangible property that is held, issued or owed in the course of a holder's business."[11] The 1981 Uniform Act provides that the property must be "*payable or distributable*" in order for it to be treated as abandoned property.[12]

This means that the holder must have an enforceable statutory or contractual payment obligation to the apparent owner, with the holder having received legal consideration from the apparent owner and all conditions precedent of the holder's commercial transaction with the owner having been satisfied, before the holder can owe a fixed and liquidated liability to the owner that might constitute abandoned property. If the holder's liability is disputed or otherwise remains uncertain, it cannot give rise to abandoned property. For example, a line of cases holds that an uncashed check or draft issued by a property and casualty insurance company as an offer of settlement of a claim under an insurance policy is *not* presumed abandoned, regardless of how long the check or draft has remained outstanding, because the insured's failure to accept the settlement offer means that the insurance company does not owe a fixed and liquidated liability to its insured.[13]

The touchstone, then, of all abandoned property laws is that the state's rights in the unclaimed property item are derivative of what the apparent owner would be able to claim from the holder. That is a sound theory that has not always prevailed in practice.

The State Unclaimed Property Life Insurance Cases

One of the earliest state unclaimed property decisions of the U.S. Supreme Court is *Connecticut Mutual Life Insurance Co. v. Moore,*[14] which rejected a constitutional challenge by nine nondomiciliary life insurance

corporations to a claim by New York to custody of the proceeds of insurance policies that the life insurance corporations had issued for delivery in New York on the lives of insureds who resided in New York.[15] Section 700 of the New York Abandoned Property Law stated at that time that monies held or owing by life insurance corporations with respect to the following three types of policies issued on the lives of New York residents were deemed abandoned: (1) matured endowment policies that had been unclaimed for seven years; (2) policies payable at death where the insured, if living, had attained the limiting age under the mortality table on which the reserves for the policy were based (an age ranging from 96 to 100) and no transaction had occurred with respect to the policy for seven years; and (3) policies payable at death where the insured was known to have died and the beneficiary of the policy had not submitted a claim for the policy proceeds for seven years.[16] The plaintiff insurance companies filed a declaratory judgment action in New York state court seeking to have the New York Abandoned Property Law declared invalid as applied to them because they were incorporated in states other than New York, and it was possible that the beneficiaries who would be entitled to receive payment of the insurance policy proceeds also resided outside New York.

The *Connecticut Mutual Life Insurance* case is usually cited for the Supreme Court's jurisdictional holding that, applying a due process "contacts" analysis, New York had the constitutional power to take custody of unclaimed monies owed to New York residents on life insurance policies issued for delivery in New York by life insurance corporations incorporated outside New York, but doing business in the state.[17] The plaintiff insurance corporations vigorously argued that only their respective states of incorporation should be able to claim custody of the insurance policy proceeds, but the Supreme Court sidestepped that argument by observing that the "problem of what another state than New York may do is not before us."[18] Just three years later, the Supreme Court held in *Standard Oil Co. v. New Jersey* that the holder's state of incorporation also had sufficient due process contacts to take custody of items of unclaimed property that the holder's owed to persons residing in other states.[19] The Supreme Court finally sorted out this jurisdictional question of which state is entitled to claim custody of an item of unclaimed property from the holder by fashioning the *Texas v. New Jersey* priority rules previously mentioned.[20]

For purposes of this column, however, the more interesting aspect of the *Connecticut Mutual Life Insurance Co.* case was the Contracts Clause argument that by allowing the state to claim custody of the insurance policy proceeds without technically complying with all of the terms of the insurance policy, the New York Abandoned Property Law was "transform[ing] into a liquidated obligation an obligation which was previously only conditional."[21] The Supreme Court acknowledged that this was the case:

> [T]he policy terms provide that the insurer shall be under no obligation until proof of death or other contingency is submitted and the policy surrendered. [The insurance corporations] contend that in dispensing with these conditions the statute transforms an obligation which is merely conditional into one that is liquidated. They further claim that unless proof of death or other contingency is submitted, they will have difficulty in establishing other complete or partial defenses, such as the fact that the insured understated his age in his application for insurance, that the insured died as a result of suicide, military service, or aviation, and that the insured was not living and in good health when the policy was delivered.[22]

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The Supreme Court concluded, however, that "these enforced variations from the policy provisions" did not violate the Contracts Clause, because "[w]hen the state undertakes the protection of abandoned claims, it would be beyond a reasonable requirement to compel the state to comply with conditions that may be quite proper as between the contracting parties. The state is acting as a conservator, not as a party to a contract."[23] It was probably not lost on the Justices that had the beneficiaries of the unclaimed insurance policy proceeds been more attentive, they almost certainly would have submitted the death certificate or other documentation required by the terms of the insurance policy to receive payment of the policy proceeds. Finding that the insurance policy proceeds were fairly classified as abandoned by the beneficiaries, the Supreme Court reasoned that the "fact that claimants against the companies would under the policies be required to comply with certain policy conditions does

not affect our conclusion. The state may more properly be custodian and beneficiary of abandoned property than any person."[24] The bottom line was that the Supreme Court was unwilling to put the state through all of the procedural requirements of the insurance policy so as to allow "the insurance companies [to] retain monies contracted to be paid on condition and which normally they would have been required to pay."[25]

[S]tate abandoned property administrators do not have a … free hand to sidestep terms and conditions of a life insurance policy in order to assert a claim to … the proceeds … on behalf of the beneficiary.

But state abandoned property administrators do not have a completely free hand to sidestep terms and conditions of a life insurance policy in order to assert a claim to custody of the proceeds of that policy on behalf of the beneficiary. The recent case of *West Virginia ex rel. Perdue v. Nationwide Life Insurance Co.*[26] presented the statutory question of whether a life insurance company could be required under the West Virginia Uniform Unclaimed Property Act (the "UPA") to conduct annual examinations of the Social Security Administration's Death Master File (the "DMF") to determine whether the insurance company was holding unclaimed insurance policy proceeds payable to beneficiaries with last known addresses in the state. Under the UPA, life insurance policy proceeds are presumed abandoned "three years after the obligation to pay arose or, in the case of a policy or annuity payable upon proof of death, three years after the insured has attained, or would have attained if living, the limiting age under the mortality table on which the reserve is based."[27] John Perdue, the West Virginia State Treasurer, filed 69 lawsuits against life insurance companies doing business in West Virginia claiming that those companies were required under the UPA to proactively review the DMF each year to determine whether insureds with West Virginia residential addresses had died or were three years past the applicable limiting age that would cause the policy to be payable and give rise to an unclaimed property reporting obligation to the state.[28]

Meanwhile, the West Virginia Insurance Code required that certain standard provisions be included in all insurance policies sold in West Virginia, including "a provision that when a policy shall become a claim by the death of the insured, settlement shall be made upon receipt of due proof of death.[29] The West Virginia Supreme Court of Appeals had previously interpreted this Insurance Code provision as conditioning the insurance company's payment obligation on the insurance policy upon the beneficiary having presented a valid claim to the insurance company for payment of the proceeds of the policy.[30]

The West Virginia Circuit Court held in the *Nationwide Insurance Co.* case that the "obligation to pay" standard of Section 36-8-2(a) of the UPA should be interpreted consistently with the long-standing "receipt of due proof of death" standard of the West Virginia Insurance Code because the West Virginia legislature had not provided otherwise when it enacted the UPA in 1997.[31] The circuit court reasoned that it was unnecessary under the UPA for a life insurance company to consult the DMF annually to determine whether the insured had died because the insurance company was subject to the requirement to escheat the insurance policy proceeds three years after the insured had reached the applicable limiting age, and the insurance company's records would include the insured's date of birth needed to make the limiting age determination. Therefore, the circuit court concluded, "[i]n the absence of due proof of death, life insurance proceeds are not presumed abandoned under the UPA until three years after the insured reaches the applicable limiting age. Under the UPA, the two statutory triggers for the unclaimed property dormancy period are receipt of due proof of death and the limiting age."[32] This holding, the circuit court noted, was supported by recent decisions of courts in Florida and Ohio.[33]

The state treasurer argued that, pursuant to Section 36-8-2(e) of the UPA, "property is payable or distributable for purposes of this column notwithstanding the owner's failure to make payment or present an instrument or document otherwise required to obtain payment," preventing the defendant life insurance companies from retaining the insurance policy proceeds in the absence of a claim by the beneficiary.[34] But the circuit court rejected their argument, observing that:

> Insurance death benefits, however, are inherently different from other types of unclaimed property. The threshold question of whether the insurer has any liability is contingent upon the happening of an event, the occurrence of which must be proven. Instead, a claimant must show that the insured has died while the policy is in force arising from a cause that is not excluded from coverage. See W. Va. Code §33-13-25

(listing limitations that may be included in insurance contracts conditioning the insurance company's responsibility to pay proceeds to a beneficiary, such as in the case of suicide). *As a result, the "due proof of death" requirement is not a mere administrative requirement for collecting an obligation that is already fixed and certain. Rather, it is an essential ingredient for creating the obligation (i.e. the "property") in the first place.*[35]

The West Virginia circuit court gave greater significance to the insurance policy term requiring the submission of a death certificate for the insured than the U.S. Supreme Court did in the *Connecticut Mutual Life Insurance Co.* case. The circuit court distinguished *Connecticut Mutual Life Insurance Co.* on the grounds that it addressed a constitutional Contracts Clause challenge, whereas the *Nationwide Insurance Co.* case raised the statutory question of whether the state abandoned property administrator had the authority to require the insurance company holder to review the DMF when that requirement was not found in either the terms and conditions of the insurance policy or the West Virginia Insurance Code. It also appears that the insureds in the *Connecticut Mutual Life Insurance* case had reached the limiting age of their policies, arguably making it unnecessary for the state to prove its unclaimed property claim by submitting death certificates for the insureds. Anyway, the circuit court held that the state treasurer had overstepped his statutory authority by administratively inserting this DMF review requirement in the West Virginia unclaimed property laws.[36]

Reporting the Cash Value of Merchandise-Only Gift Certificates or Gift Cards

Many merchants sell merchandise-only gift certificates or gift cards that are not redeemable for cash, except when required by state consumer protection laws (*e.g.*, when a small balance remains on the gift card). Even though the apparent owner would not be able to claim a payment of cash from the merchant for the redeemed gift card, state abandoned property administrators typically require that holders escheat the cash value of the merchandise-only gift certificate/card, pointing to the 1981 Uniform Act provision stating that "[i]n the case of a gift certificate, the amount presumed abandoned is the price paid by the purchaser for the gift certificate."[37] The 1995 Uniform Act has a similar provision stating that for gift certificates "the amount abandoned is deemed to be 60 percent of the certificate's face value."[38]

Again, because the state is asserting a derivative claim to the apparent owner's property rights in the merchandise-only gift certificate, one might assume that the state may not rewrite the terms of the gift certificate to claim custody of the cash value of the instrument. The Tennessee Chancery Court so held in 2001 in *Service Merchandise Co. v. Adams.*[39] Service Merchandise Company, a Tennessee corporation headquartered in Brentwood, Tennessee, sold gift certificates that were redeemable only for merchandise purchased at a Service Merchandise retail store or through the Service Merchandise mail-order department. According to the express terms of the gift certificate, the bearer of the instrument was not entitled to redeem the gift certificate for cash or use it to pay a credit balance owed to Service Merchandise. If a redeemed gift certificate had a remaining balance of $10 or more, Service Merchandise would issue the apparent owner another gift certificate for the remaining balance. A remaining balance of less than $10 would be paid out in cash.[40]

The Tennessee state treasurer audited Service Merchandise and demanded a cash payment of $406,133 as the estimated face value of all of the unredeemed gift certificates outstanding for more than five years on Service Merchandise's books, pursuant to Tennessee's Unclaimed Property Act. For periods prior to 1993, the Tennessee state treasurer claimed the face value of the unredeemed gift certificates pursuant to the miscellaneous unclaimed property provision of the Act and a regulation that treated unredeemed gift certificates as miscellaneous property subject to the Unclaimed Property Act.[41] For 1993 and thereafter, the state treasurer based his demand for cash equal to the face value of the unredeemed gift certificates on Tennessee's version of the 1981 Uniform Act provision previously discussed.[42]

The Tennessee Chancery Court accepted Service Merchandise's argument that the state treasurer was impermissibly changing the terms of the gift certificate by asserting a claim to a cash value of the gift certificates:

> According to the undisputed facts, the Plaintiff's customers purchase gift certificates for an amount certain. In consideration of the price paid, the Plaintiff promises to deliver to the bearer of the gift certificate, upon redemption, merchandise with a retail sales price up to and including the amount specified on the certificate. The bearer of the gift certificate ("Owner"), by contract, enjoys no expectation of the cash equivalent of the amount specified on the certificate. In other words, the gift certificate, by contract, does not represent a cash value. Rather, the gift certificate represents the legal interest of the Owner in

> the fulfillment by Plaintiff of its obligation to deliver merchandise, available at the Plaintiff's showrooms or by mail order, with a sales price up to and including the amount specified on the certificate. The Plaintiff's obligation of contracts is an intangible promise to deliver merchandise in exchange for the gift certificate. There being no dispute as to material fact, the Court holds that, for the purposes of the Act, the property, as embodied in the gift certificate, is, as a matter of law, the intangible promise of the Plaintiff (Holder) to deliver merchandise to the Owner.[43]

The Tennessee Chancery Court determined that the "amount presumed abandoned" language of Section 66-29-135(a) of the Tennessee Code merely provided a valuation of the intangible promise by Service Merchandise to deliver merchandise to the owner of the gift certificate rather than a statutory obligation of Service Merchandise to deliver the cash purchase price of the gift certificate to the state.[44]

The Tennessee Chancery Court further held that if Section 66-29-135(a) were to require Service Merchandise to deliver cash equal to the face value of the unredeemed gift certificates, it would violate the Takings Clause of the U.S. Constitution by denying Service Merchandise its anticipated gross profit from selling merchandise in exchange for a redeemed gift certificate.[45] Requiring Service Merchandise to escheat cash equal to the face value of the unredeemed gift certificate would also have violated the Contracts Clause of the U.S. Constitution, according to the Chancery Court, by rewriting Service Merchandise's contractual obligation to delivery merchandise in exchange for the redeemed gift certificate.[46]

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Unfortunately, this is not the universal view of the courts on this issue. In *Benson v. Simon Property Group, Inc.,*[47] the Georgia Supreme Court reviewed the 1981 Uniform Act provision on gift certificates and held that "[i]n light of the purpose of this statute to utilize unclaimed gift certificates for the benefit of all the people of the state, its meaning is simply that an amount equal to the price part for an unclaimed gift certificate must be paid to the state after five years, regardless of whether the certificate previously expired or otherwise lost value pursuant to contractual terms."[48] The New York Supreme Court (the state trial court) had reached a similar conclusion the previous year in *Kimberly's A Day Spa v. Hevesi.*[49]

In *New Jersey Retail Merchants Association v. Sidamon-Eristoff*,[50] the United States Court of Appeals for the Third Circuit addressed the constitutionality of a 2010 amendment ("Chapter 25") of the New Jersey Unclaimed Property Law that made stored-value cards ("SVCs") or gift cards escheatable after only *two* years of inactivity.[51] The Third Circuit noted that for nearly 15 years prior to the enactment of Chapter 25, gift certificates and similar instruments had not been treated as unclaimed property in New Jersey based on a decision of the New Jersey appellate court.[52] The Third Circuit explained that:

> The key reason New Jersey did not escheat gift certificates was that they were not redeemable for cash. *Id.* at 1179-80. If the State were to escheat gift certificates, the issuers would have had to turn over the value of the gift certificates in cash to the State, when they were originally bound to turn over only merchandise or services to the owner. *Id.* at 1179. The Superior Court of New Jersey found that the State's escheat law was not intended to "impose an obligation different from the obligation undertaken to the original owner" of the gift certificate. *Id.* at 1180.[53]

The New Jersey Unclaimed Property Division applied Chapter 25 retroactively to all SVCs that had been inactive for two years. Issuers of such dormant SVCs were required to report and deliver cash equal to the remaining balance of the SVC to the state.

The Third Circuit affirmed the district court's determination that the retroactive application of Chapter 25 to merchandise-only SVCs violated the Contracts Clause of the U.S. Constitution, because "Chapter 25 operate[d] as a substantial impairment on the contractual relationships of SVC Issuers."[54] The Third Circuit reasoned that:

> The contractual agreement between SVC Issuers and purchasers provides that the balance on the gift card may be redeemed only for merchandise or services; thus, Issuers of closed loop SVCs expected to realize a profit when the bearer redeemed the card for the Issuers' merchandise or services, and the Issuers of open loop SVCs expected to realize a merchant fee, which is a fee Issuers like Amex retained from retailers, when

the bearer redeemed the card from retailers that accept open loop SVCs. [Citation omitted.] Chapter 25 requires SVC Issuers to submit the value of the SVCs *in cash* to the State at the end of the abandonment period, even though the SVCs are not redeemable for cash under the SVC Issuers' contract with the customer. Because the value of the SVCs includes the expected profit or merchant fee, requiring SVC Issuers to turn over the entire value of the SVC in cash effectively transfers their expected benefits to state custody. By imposing such an unexpected obligation on SVC Issuers, Chapter 25 impaired their contractual relationship.[55]

Nor, in the Third Circuit's view, was this a trivial change of the terms of the SVC:

> SVC Issuers' reliance on the expected profit or merchant fee was vital to their contractual relationships; the expected benefits supported the administrative cost of issuing and processing SVCs and allowed them to issue SVCs without charging the purchaser additional fees beyond the face value of the gift cards. Moreover, Chapter 25 imposed retroactive obligations on SVC Issuers that were unanticipated because New Jersey law never before provided for the escheat of SVCs. Therefore, Chapter 25 substantially impaired the SVC Issuer's contractual relationship by imposing unexpected obligations in an area where reliance is vital.[56]

For this reason, the Third Circuit upheld the district court's preliminary injunction against the *retroactive* application of Chapter 25 to existing merchandise-only SVCs. Going forward, however, issuers of SVCs had been put on notice that they could be required to escheat the unredeemed balance of an SVC in cash to New Jersey. The Third Circuit did not seem to view the *prospective* application of the Chapter 25 to merchandise-only SVCs as violating the Contracts Clause because issuers of such SVCs should not be relying on being able to retain the remaining balance of the stored value card when they priced the card. In 2012, the New Jersey legislature amended Section 46:30B-42.1 to require that a holder report 60 percent of the balance of a merchandise-only SVC that had been issued on or after July 1, 2010 (the date of enactment of the 2010 gift card provision invalidated in the *New Jersey Retail Merchants Association* case) and remained unclaimed for five years.[57]

State "Anti-Limitations" or "Private Escheat" Statutes

Section 29(a) of the 1981 Uniform Act provides that:

> The expiration, before or after the effective date of this Act, of any period of time specified by contract, statute or court order, during which a claim for money or property can be made or during which an action or proceeding may be commenced or enforced to obtain payment of a claim for money or to recover property, does not prevent the money or property from being presumed abandoned or affect any duty to file a report or to pay or deliver abandoned property to the administrator as required by this Act.[58]

The Commissioners' Comment to this "anti-limitations" provision in the 1981 Uniform Act flatly states that it is intended to ensure that "the expiration of time periods set forth in contracts will not prevent the property from becoming reportable" under the state's abandoned property law. The 1995 Uniform Act includes the same "anti-limitations" provision.[59]

This anti-limitations provision is an unfortunate example of legislative overreaction to three unclaimed property cases in which the court invoked "public policy" to prevent the holder from relying on a contractual time period that the holder had unilaterally adopted for the purpose of circumventing the state's unclaimed property laws. As the legal maxim states, "bad facts make bad law."

The first of these cases is *New Jersey v. Jefferson Lake Sulphur Co.*,[60] which presented the question of whether a New Jersey corporation could avoid having to report unclaimed dividends under the new New Jersey abandoned property law because of an amendment to the corporation's charter providing that, where a shareholder did not claim his dividend payment for three years, the funds that the corporation had set aside for that dividend payment would revert in full ownership to the corporation and would no longer be owed to the shareholder.[61] About four months after New Jersey adopted its custodial escheat law in 1951, the board of directors of Jefferson Lake Sulphur Company asked the corporation's shareholders to approve this amendment, in what the New Jersey Supreme Court described as being "a frankly admitted effort to circumvent the application of the Custodial Escheat Law."[62] Immediately after the shareholders of Jefferson Lake Sulphur approved the amendment, the directors of the company transferred about $5,600 of unclaimed dividend funds to the company's earned surplus.[63]

About six years later, the New Jersey Attorney General prevailed in an action that he brought against Jefferson Lake Sulphur to claim payment of the unclaimed dividends under the state's custodial escheat law. The New Jersey Supreme Court held that under New Jersey's corporation laws, when the company declared a dividend and specifically set aside funds in a separate bank account for payment of the dividends, the funds became the property of the shareholders to whom the dividends were payable. As the New Jersey Supreme Court put it, "[s]uch moneys once so separated from the general assets of the entity are trust funds for the payment of the dividend and cannot be diverted by it for any other purpose."[64] The New Jersey Supreme Court went on to observe that the New Jersey legislature had declared the "public policy" of the state to be that unclaimed moneys should be used for the benefit of all the citizens of New Jersey through the operation of its custodial escheat law and that the "[a]lteration of a charter for the avowed purpose of defeating a relevant aspect of the sovereign's declared public policy cannot achieve judicial approval."[65] Notwithstanding this invocation of public policy, the crux of the *Jefferson Lakes Sulphur* case was that under the applicable New Jersey corporation laws, the corporation still owed an outstanding liability to the shareholders who had not claimed their dividend payments, regardless of the forfeiture provision in the corporation's charter, and it was that outstanding liability that gave rise to unclaimed property reportable to New Jersey.

The anti-limitations provision in state abandoned property laws is the most egregious departure from the derivative claim principle.

About 17 years later, this public policy argument surfaced again in *Screen Actors Guild, Inc. v. Cory*.[66] In that case, a labor union bylaw provision expressly provided that if a member did not claim his or her residual payment within a six-year period, the funds associated with that residual payment would automatically be assigned to the union for the use of its membership as a whole.[67] It is questionable whether the members of the Screen Actors Guild had meaningfully consented to being subject to this forfeiture provision in the union's bylaws because membership in the union was a requirement for obtaining many jobs in the entertainment industry. The California Court of Appeals also noted that, in practice, the Screen Actors Guild did not enforce this bylaw forfeiture provision against its members.[68] But the California Court of Appeals cited *Jefferson Lakes Sulphur* for the proposition that the bylaw provision was "void as a private escheat law obviously designed to frustrate the operation of the [California Unclaimed Property Law]."[69]

In *People ex rel. Callahan v. Marshall Field & Co.*,[70] a department store company sold gift certificates with a 10-year expiration date at a time when Illinois utilized a 15-year statutory dormancy period under its abandoned property law to escheat unredeemed gift certificates and other types of unclaimed property.[71] When the Illinois General Assembly shortened the general statutory dormancy period to seven years in 1975, Marshall Field immediately responded by reducing the expiration date on its gift certificates to five years.[72] Marshall Field's took the position in litigation against the Illinois Department of Financial Institutions that the expired gift certificates did not give rise to unclaimed property because the company had ceased to owe a payment obligation to the owner of the gift certificate two years before the instrument was presumed abandoned under the Illinois abandoned property law. Citing *Jefferson Lake Sulphur* and *Screen Actors Guild*, the Illinois Appellate Court held that "where a private agreement between the parties is in fundamental conflict with public policy as established by the legislature, the private agreement must fall .... [T]he holder's theory here would result in a private escheat law whereby the holder rather than the State would enjoy the benefit of the unclaimed property. Such a result would be contrary to the obvious purpose and policy of the [Illinois Abandoned Property] Act."[73] The appellate court's opinion was undoubtedly influenced by the changes that Marshall Field had made to its gift certificates in response to the revisions to the Illinois abandoned property laws.

If the anti-limitations provision of the 1981 and 1995 Uniform Acts were given a literal interpretation, it would appear to allow a state abandoned property administrator to set aside any sort of contractual limitations provision, even if the contractual limitations provision serves a valid business purpose, was agreed to by the holder's customer or vendor and was consistently applied by the holder in its commercial transactions. Such an expansive application of the "anti-limitations" provision would not be supported by the holdings of the *Jefferson Lake Sulphur*, *Marshall Field* and *Screen Actors Guild* cases. Moreover, it would be contrary to the fundamental principles of state abandoned property laws. Contractual limitations provisions often are important terms in commercial transactions that affect the economics of the transaction. If the holder struck a bargain

with its customer or vendor, it is difficult to see why the state should be allowed to invoke its abandoned property laws to claim the benefit of the bargain that was supposed to inure to the holder under the terms of the commercial transaction between the holder and its customer or vendor. After all, state abandoned property laws are intended to prevent unjust enrichment of the holder and to reunite the owner with property that it would be entitled to claim directly from the holder, not to extract a penalty from the holder as a result of the owner's decision not to complete a transaction in a timely manner.

This is not to say that state abandoned property administrators should be denied the authority to disregard a contractual limitations provision that a holder has unilaterally imposed on its customer or vendor for the sole purpose of avoiding its compliance obligations under state abandoned property laws. Those types of contractual limitations provisions would violate public policy. Moreover, a holder that unilaterally imposes a contractual limitation provision on its customers or vendors, or does not bring the contractual limitations provision to the attention of the customer or vendor when the commercial transaction is entered into, probably should not be able to enforce the contractual limitation provision against the customer or vendor under the state's contract laws or consumer protection laws—or, by extension, the state under its abandoned property law. This is the scenario that the courts addressed in *Jefferson Lake Sulphur, Marshall Field's* and *Screen Actors Guild*, and it is the scenario to which the "anti-limitations" provisions of the 1981 and 1995 Uniform Acts should be limited.

It is quite another matter, however, for a state abandoned property administrator to assert that unclaimed property exists in a situation where a customer or vendor understood that it would be subject to a contractual limitation provision when it entered into a commercial transaction with the holder, the holder regularly enforces the contractual limitation provision against its customers or vendors, and the contractual limitation provision is reasonable and serves a valid business purpose. Under those circumstances, a court should conclude, as a matter of contract law, that the contractual limitation provision reduced or eliminated the holder's liability to the customer or the vendor. If the contractual limitation provision is respected for purposes of determining whether the holder owes a liability to the customer or the vendor, the contractual limitation provision should also be respected for purposes of determining whether the holder has liability under state abandoned property laws. The holdings of *Jefferson Lake Sulphur, Marshall Field's* and *Screen Actors Guild*, and a properly interpreted "anti-limitations" provision, simply do not justify the state abandoned property administrator disregarding a contractual limitation provision that was adopted for a valid business purpose rather than to circumvent the state abandoned property laws. It does not appear that the courts have yet considered the unclaimed property consequences of a contractual limitations period with a business purpose and substantial economic substance.

Conclusion

While exceptions occasionally arise to the principle that a state's right to claim custody of an unclaimed property item is derivative of the apparent owner's rights in that property item, this remains the guiding principle of state abandoned property laws. It is understandable that the U.S. Supreme Court concluded in the *Connecticut Mutual Life Insurance Co.* case that requiring the state of New York to produce death certificates for all of the insureds would be a cumbersome procedural burden for the state and probably frustrate the purpose of the state's abandoned property law. This has been viewed as a narrow procedural exception to the derivative claim aspect of state abandoned property laws. The recent *Nationwide Life Insurance Co.*, *MetLife* and *John Hancock Life Insurance Co.* cases involving state claims that life insurance companies are required to conduct annual reviews of the death master file to identify deceased insureds demonstrate that courts have not set aside the derivative claim principle in applying state abandoned property laws to life insurance companies.

It is also understandable that state abandoned property administrators would prefer to claim custody of the cash value of unredeemed gift certificates or gift cards rather than receive replacement certificates or cards that may not be very useful to the state. Unless the state abandoned property administrator could turn the replacement certificates/cards into cash by selling them on a secondary market, the replacement certificates would probably sit unused on a shelf in the state abandoned property administrator's office. Nevertheless, it would be more consistent with the derivative claim principle for the state administrator to receive replacement gift certificates, and the analysis of the *Service Merchandise* case supports that view. The *New Jersey Retail Merchants Association* case recognized the unfairness of allowing states to claim custody of the cash value of merchandise-only gift certificates and stored value cards, too, at least on a retroactive basis.

The anti-limitations provision in state abandoned property laws is the most egregious departure from the derivative claim principle. While the *Jefferson Lake Sulphur, Screen Actors Guild* and *Marshall Field Co.* cases probably reached the correct result in rejecting attempts by holders

to unilaterally implement a contractual time period for the sole purpose of circumventing the state's abandoned property law, these cases do not stand for the broad proposition that all expiration dates and other contractual limitations periods can be ignored by state abandoned property administrators. The anti-limitations provision is inartfully drafted and needs to be enforced with common sense. Hopefully, courts will do so when called upon to interpret a contractual time period or term that had a valid business purpose and substantial economic substance in the commercial transaction between the holder and the apparent owner of the unclaimed property item.

At the end of the day, then, state abandoned property laws should be administered and enforced consistently with the derivative claim principle. To cast the abandoned property laws adrift from this guiding principle could lead to illogical and arbitrary results.

ENDNOTES

[1] Statutory dormancy periods vary by state and by the type of unclaimed property at issue. These periods currently range from as short as one year for uncashed payroll checks to three to five (or even 15) years for other types of unclaimed property. States continue to shorten their dormancy periods in order to accelerate the holder's reporting of unclaimed property to the state.

[2] The three uniform acts are the 1954 Uniform Disposition of Unclaimed Property Act, which was revised in 1966; the 1981 Uniform Unclaimed Property Act; and the 1995 Uniform Unclaimed Property Act.

[3] Although the likelihood of the owner actually presenting a claim for payment of the unclaimed property is remote, state abandoned property laws are designed to provide the apparent owner some notice of his or her right to claim the property from the holder or the state. All three of the Uniform Acts require the holder, before filing its annual report with the state, to send written "due diligence" notices to apparent owners of unclaimed property if the holder has a record of a last known address of the apparent owner and the property has the requisite value. *See* 1995 Uniform Act §7(e) (holder must send a due diligence letter to the apparent owner of unclaimed property valued at $50 or more, 60 to 120 days before the date on which the holder will file the annual report); 1981 Uniform Act §17(e) (holder must send a due diligence letter to the owner of unclaimed property valued at $50 or more, up to 120 days before the date on which the holder will file the annual report); 1954/1961 Uniform Act §11(e) (if the holder knows of the whereabouts of the apparent owner of unclaimed property, and if the owner's claim to the property is not barred by a statute of limitations, the holder is required to "communicate with the owner and take necessary steps to prevent abandonment from being presumed"). The annual report that the holder files with the state includes the names and last known addresses of owners who did not respond to the holder's due diligence notices. 1995 Uniform Act §7(b); 1981 Uniform Act §17(b); 1954/1961 Uniform Act, §11(b). The state abandoned property administrator then publishes this information in a newspaper of general circulation in the area where the owner's last known address is located. 1995 Uniform Act §9; 1981 Uniform Act §18; 1954/1961 Uniform Act §12. Many states now also make this information available to owners on the state's web site.

[4] *Texas v. New Jersey*, SCt, 379 US 674, 85 SCt 626 (1965).

[5] *Delaware v. New York*, SCt, 507 US 490, 113 SCt 1550 (1993).

[6] Under Section 1(11) of the 1981 Uniform Act, an owner's last known address is an address that is sufficient to deliver mail to the owner. The 1995 Uniform Act relaxes this rule to require only some indication in the holder's records that the owner's last known address was located in a particular state. *See* Commissioners' Comment to Section 1 of the 1995 Uniform Act.

[7] The 1981 and 1995 Uniform Acts have added a third priority rule, the so-called "transactional rule," which allows the state where the transaction occurred that gave rise to the unclaimed property item to claim the property if neither the state of the owner's last known address nor the holder's state of corporate domicile will lay claim to the property item under its abandoned property laws. *See* 1995 Uniform Act §4(6); 1981 Uniform Act §3(6). Because all of the states have now enacted abandoned property laws, the transactional rule would come into play only in situations where the unclaimed property item qualifies for an exemption in the abandoned property law of the holder's state of corporate domicile (and possibly the abandoned property law of the owner's state, too). In *New Jersey Retail Merchants Association v. Sidamon-Eristoff*, CA-3, 699 F3d 374 (2012), *cert. denied*, 133 SCt 528 (2012), the U.S. Court of Appeals for the Third Circuit held that the transactional rule is preempted by the Supreme Court's priority rules in *Texas v. New Jersey* because New Jersey, the transactional rule state, was impermissibly disregarding the exemption of the higher ranking state of the holder's state of corporate domicile for the unredeemed gift cards to which New Jersey was laying claim.

[8] *See* 1995 Uniform Act §1(4); 1981 Uniform Act §1(6). Arguably, the state of "corporate domicile" of a holder organized as a limited partnership or a limited liability company should be its state of organization. *See* John A. Biek, State Law & State Taxation Corner, *States Update Their Rules for State Abandoned Property Reporting by Passthrough Entity Holders*, J. Passthrough Entities, Jan.–Feb. 2005, at 15.

[9] 1981 Uniform Act §1(10) (definition of "intangible property").

[10] 1995 Uniform Act §1(13) (definition of "property").

[11] 1995 Uniform Act §1(13) (emphasis added).

[12] 1981 Uniform Act §2 (emphasis added).

[13] *See, e.g., Aetna Casualty & Ins. Co. v. Alabama*, 414 So2d 455, 460 (Ala. 1982); *Allstate Ins. Co. v. Eagerton*, 403 So2d 173 (Ala. 1981); *Insurance Co. of N. Am. v. Knight*, 291 NE2d 40, 45 (Ill. Ct. App. 1972), *app. dismissed*, SCt, 414 US 804 (1973); *Kane v. Insurance Co. of N. Am.*, 392 A2d 325, 329 (Pa. Comm. Ct. 1978). *See also* Commissioners' Comment to Section 2 of the 1981 Uniform Act.

[14] *Connecticut Mutual Life Insurance Co. v. Moore*, SCt, 333 US 541, 68 SCt 682 (1948).

[15] *Id.* at 542.

[16] *Id.* at 543–44.

[17] *Id.* at 548.

[18] *Id.*

[19] *Standard Oil Co. v. New Jersey*, SCt, 341 US 428, 435–36 (1951).

[20] *Texas v. New Jersey*, SCt, 379 US 674, 85 SCt 626 (1965).

[21] *Connecticut Mutual Life Insurance Co.,* 333 US at 545.

[22] *Id.* at 545–55.

[23] *Id.* at 547.

[24] *Id.*

[25] *Id.* at 546

[26] *West Virginia ex rel. Perdue v. Nationwide Life Insurance Co.*, No. 12-C-287 through 12-C-296, 12-C-322 through 12-C-331, 12-C-355 through 12-C-364, 12-C-372 through 12-C-381, 12-C-419 through 12-C-447 (W. Va. Cir Ct. of Putnam County, Dec. 27, 2013).

[27] W. Va. Code §36-8-2(a)(8).

[28] *Nationwide Life Insurance*, slip op. at 2.

[29] W. Va. Code §33-13-14.

[30] *Nationwide Life Insurance*, slip op. at 6 (citing *Petrice v. Federal Kemper Insurance Co.*, 163 W. Va. 737, 739-40, 260 SE2d 276, 278 (1979) ("the furnishing of a proof of claim" is a "condition precedent to recovery")).

[31] *Nationwide Life Insurance*, slip op. at 7.

[32] *Id.*, slip op. at 8.

[33] *See Total Asset Recovery Services LLC v. MetLife, Inc.*, No. 2010-CA-3719 (Fla. Cir. Ct., Aug. 20, 2013) ("Florida has not adopted a law requiring Prudential to consult the Death Master File, avered by TARS, in connection with payment or escheatment of life insurance benefits. Likewise, Florida has adopted no law imposing an obligation on Prudential to engage in elaborate data mining of external databases … in connection with payment on escheatment of life insurance benefits"); *Andrews v. Nationwide Mutual Insurance*

Co., 2012 Ohio App. LEXIS 4318 (Ohio Ct. App., Oct. 25, 2012) ("a finding obligating [the life insurance company] to solicit or gather information pertaining to an insured's death would be contrary to the terms contained in the insurance policy," rather, the law "place[s] the burden on the claimant or the beneficiary to produce the proof of death"). *See also Feingold v. John Hancock Life Insurance Co.* No. 1:13-cv-10185-JLT (D. Mass. 2013) (dismissing a class action lawsuit alleging the insurance company had breached its duty to consult the DMF).

[34] *Nationwide Insurance Co.*, slip op. at 9 (emphasis added).

[35] *Id.*, slip op. at 10–11 (emphasis added).

[36] The National Conference of Insurance Legislators ("NCOIL") has drafted a model act requiring an insurance company to check its in-force life insurance policies against the DMF to determine if either the social security number or the name and date of birth of the insured match information in the DMF. If so, the insurance company is given 90 days to verify the death of the insured, determine what benefits are payable, and locate any beneficiaries. If the insurance company is unable to confirm this information, the insurance company must escheat the insurance proceeds when the applicable dormancy period has passed. To date at least nine states, including Alabama, Kentucky and Maryland, have enacted DMF review laws based on or similar to the NCOIL model act.

[37] 1981 Uniform Act §14(b).

[38] 1995 Uniform Act §2(a)(7).

[39] *Service Merchandise Co. v. Adams*, No. 97-2782-III (Tenn. Chanc. Ct., June 29, 2001), [Tenn.] St. Tax Rep. (CCH) ¶ 400-810.

[40] *Id.,* slip op. at 24,042.

[41] Tenn. Code §66-29-112; Tenn. Comp. Regs. 1700-2-1.18(1)(f)(1979).

[42] Tenn. Code §66-29-135(a).

[43] *Service Merchandise Co.*, slip op. at 24,044.

[44] *Id.*, slip op. at 24,045.

[45] *Id.*

[46] *Id.*, slip op. at 24,046.

[47] *Benson v. Simon Property Group, Inc.*, 281 Ga. 744, 642 SE2d 687 (2007).

[48] *Id.* at 691.

[49] *Kimberly's A Day Spa v. Hevesi*, 11 Misc. 3d 954, 810 NYS2d 616, 618 (Sup. Ct. 2006).

[50] *New Jersey Retail Merchants Association v. Sidamon-Eristoff*, CA-3,669 F3d 374 (2012), *cert. denied*, 133 SCt 528 (2012).

[51] 2010 N.J. Laws, Ch. 25.

[52] *New Jersey Retail Merchants Association,* 669 F3d at 383 (*citing In re November 8, 1996 Determination of the State of New Jersey Department of Treasury, Unclaimed Property Office,* 309 N.J. Super. 272, 706 A2d 1177 (N.J. Super. Ct. App. Div. 1998)).

[53] *New Jersey Retail Merchants Association*, 669 F3d at 383-84.

[54] *Id.* at 386.

[55] *Id.* at 386–87 (emphasis in original).

[56] *Id.* at 387.

[57] 2012 N.J. Laws, Ch. 14, §1.

[58] 1981 Uniform Act §29(a).

[59] 1995 Uniform Act §19(a).

[60] *New Jersey v. Jefferson Lake Sulphur Co.*, 36 N.J. 577, 178 A2d 329 (1962).

[61] *Id.*

[62] *Id.* at 583.

[63] *Id.* at 586.

[64] *Id.* at 588 (*citing Parsons v. Standard Oil Co.*, 5 N.J. 281, 300-303 (1950)); 13 Am. Jur. Corporations §673).

[65] *Jefferson Lake Sulphur*, 36 N.J. at 588 and 591.

[66] *Screen Actors Guild, Inc. v. Cory*, 91 Cal. App. 3d 111, 154 Cal. Rptr. 77 (1979).

[67] *Screen Actors Guild, Inc. v. Cory*, 91 Cal. App. 3d at 113.

[68] *Id.* at n.1.

[69] *Id.* at 115.

[70] *People ex rel. Callahan v. Marshall Field & Co.*, 83 Ill. App. 3d 811, 404 NE2d 368 (1980).

[71] *Id.* at 817.

[72] *Id.*

[73] *Id.* at 818.