A Bridge Too Far: Due Process Considerations in State Unclaimed-Property Law Enforcement

"The UPL [Unclaimed Property Law] is not a permanent or 'true' escheat statute. Instead, it gives the state custody and use of unclaimed property until such time as the owner claims it. Its dual objectives are 'to protect unknown owners by locating them and restoring their property to them and to give the state rather than the holders of unclaimed property the benefit of the use of it, most of which experience shows will never be claimed.'"[1]

I. INTRODUCTION

Although U.S. economists note that the most recent U.S. recession came to an end in June 2009, belt tightening can still be felt throughout the economy, more than three years later.[2] Perhaps nowhere is this more evident than in state budgets, which continue to face huge shortfalls and endure significant cutbacks.[3] With legislatures generally unwilling to raise taxes to make up for these deficits, states have looked toward new sources—unclaimed property, in particular—to find much needed cash.[4]

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1. Harris v. Westly, 10 Cal. Rptr. 3d 343, 346 (2004) (quoting Douglas Aircraft Co. v. Cranston, 374 P.2d 819, 821 (Cal. 1962)).

2. *See generally* NAT'L BUREAU OF ECON. RESEARCH, REPORT OF THE BUSINESS CYCLE DATING COMMITTEE (2010), http://www.nber.org/cycles/sept2010.html. The recession began in December 2007. *See id.*

3. *See* PHIL OLIFF, CHRIS MAI & VINCENT PALACIOS, CTR. ON BUDGET AND POLICY PRIORITIES, STATES CONTINUE TO FEEL RECESSION'S IMPACT (2012), http://www.cbpp.org/files/2-8-08sfp.pdf. The Center on Budget and Policy Priorities' report notes that thirty-one states have projected or addressed shortfalls totaling $55 billion for 2013 and calculates that state budget shortfalls from 2009-2012 totaled a staggering $540 billion combined. *Id.* at 2. The cause of these deficits can be traced back to the recession that began in 2007, which this report states "caused the largest collapse in state revenues on record." *Id.* at 1; *see* Editorial, *Candidates Fail Voters by Downplaying Budget Crisis*, DALL. MORNING NEWS, Oct. 25, 2010, http://www.dallasnews.com/opinion/editorials/20101025-Editorial-Candidates-fail-voters-by-8532.ece (noting Texas's $25 billion shortfall); Nicole Lapin, *States Are in 'Crisis Mode': Washington Governor*, CNBC, Oct. 27, 2010, http://www.cnbc.com/id/39854497 ("The state of Washington is quickly running out of money."); Mike McDaniel, *Upcoming Year Could Be Worse for State's Budget Crisis*, WDAM, Oct. 18, 2010, http://www.wdam.com/Global/story.asp?S=13339261 (documenting Mississippi's estimated $800 million to $1.2 billion budget hole). Even political candidates in the current election cycle have alluded to legislation allowing states to file for bankruptcy protection. *See* Lisa Lambert, *State Bankruptcy Bill Imminent, Gingrich Says*, REUTERS, Jan. 21, 2011, http://www.reuters.com/assets/print?aid=USTRE70K6PI20110121.

4. *See* Peggy Fikac, *Texas Lawmakers Look Beyond Cuts for Revenues*, HOUS. CHRON., Mar. 7, 2011, http://www.chron.com/news/houston-texas/article/Texas-lawmakers-look-beyond-cuts-for-revenues-1687266.php (highlighting Texas Legislature's search for "revenue enhancers"). Dale Craymer of the Texas

By some accounts, $35 billion of unclaimed property is currently held by states—an amount that continues to increase annually.[5] Simply put, the transformation of unclaimed property into revenue first requires a state to "escheat," or take custody of property from a "holder," which is generally a corporation.[6] Furthermore, "unclaimed property" usually refers to intangible property (such as amounts represented by uncashed checks, amounts in suspense, or outstanding stock) in the custody of a holder that actually belongs to another (known as the "owner"), but which has been inactive for a statutorily defined amount of time (the "dormancy period").[7] In their search for revenue, states have recently been escheating more unclaimed property than ever through the use of increasingly aggressive techniques.[8] Although states do not take title to the property they recover, most state laws provide that at least some portion of funds received as unclaimed property is deposited in a state's general

Taxpayers and Research Association observed that "there is a tremendous amount of effort being invested in identifying new revenues that avoid being called a tax bill" and that "[p]olitically, a lot of members [of the legislature] have pledged not to raise taxes." *Id.* According to this article, one Texas lawmaker suggested revisions to the state unclaimed-property law that would yield an additional $72 million in revenue for Texas, but would require property to be turned over more frequently than before. *Id.*

5. *See What Is Unclaimed Property*, NAT'L ASS'N OF UNCLAIMED PROP. ADM'RS (NAUPA), http://www.unclaimed.org/what/ (last visited Sept. 27, 2012) (stating unclaimed property held by states totals at least $32.887 billion). In March 1999, the amount of unclaimed property held by states was significantly less, at approximately $10 billion. *See* Michael I. Saltzman, *Providing Protection in State Unclaimed Property Audits*, 89 TAX NOTES 1599, 1599 & n.2 (2000) (citing figure on NAUPA website at time of publication). By 2002, that number had doubled to $20 billion. *See* Stephanie Cutler et al., *What Corporate America Needs to Know About Unclaimed Property: A Primer for the Business Holder*, 54 TAX EXECUTIVE 335, 335 (2002) (highlighting value of unclaimed property in state coffers as of 2002).

6. *See generally* Cutler et al., *supra* note 5 (discussing process by which holders must report unclaimed property to states).

7. *See id.* at 335, 341 n.3 (listing escheatable property types). Escheatment occurs after a statutorily prescribed period of time has elapsed in which there was no activity or interest in the property and the holder cannot locate the owner. *Id.* at 336. Each state has adopted its own dormancy period; they are not uniform and often vary between property types. *See, e.g.*, ARK. CODE ANN. § 18-28-202 (2012) (highlighting dormancy periods ranging from one year for wages to fifteen years for traveler's checks); KAN. STAT. ANN. § 58-3935 (2012) (defining dormancy periods for various types of property); MASS. GEN. LAWS ANN. ch. 200A §§ 5-5C (2012) (highlighting specific dormancy periods for intangible interests in business associations). Although not discussed in this Note, the shortening of dormancy periods has been one technique employed by states to collect unclaimed property more quickly. *See* Fikac, *supra* note 4 (noting shortening of Texas's dormancy period as one way to raise needed revenue); *see also* Amy F. Nogid, *Budget Bill Would Reduce Dormancy Periods for Unclaimed Property*, MOFO N.Y. TAX INSIGHTS, March 2011, at 1, 6, *available at* http://www.mofo.com/files/Uploads/Images/110301-MoFo-New-York-Tax-Insights.pdf (discussing New York's proposed shortening of dormancy periods); Teagan J. Gregory, Note, *Unclaimed Property and Due Process: Justifying "Revenue-Raising" Modern Escheat*, 110 MICH. L. REV. 319, 319-26 (2011) (discussing due-process issues regarding shortening dormancy periods).

8. *See* Ed Anderson, *State to Set Record in Collecting Unclaimed Property*, NEW ORLEANS TIMES PICAYUNE, Nov. 16, 2009, http://blog.nola.com/politics/print.html?entry=/2009/11/state_to_set_record_in_collect.html (discussing Louisiana's record-breaking unclaimed-property collection); *see also Treasury's Abandoned Property Division Nets $76M in Revenue*, BELMONT CITIZEN-HERALD, Dec. 30, 2009, http://www.wickedlocal.com/belmont/news/x370505962/Treasurys-Abandoned-Property-Division-nets-76M-in-revenue ("Abandoned Property Division's stock liquidation sale and eBay auction . . . generated a combined $76.1 million in revenue for the Commonwealth.").

fund, or go so far as to direct the proceeds from unclaimed property to fund specific state programs.[9] The benefits of a state's use of unclaimed property are compounded by the fact that underlying owners, to whom the property rightfully belongs, rarely claim escheated property from the state.[10] Thus, states have begun to transform their unclaimed-property laws and regulations into revenue-raising mechanisms that undermine their original, consumer-protection-oriented goal of reuniting missing owners with their property.[11] This departure raises a host of due-process concerns for unclaimed-property holders, which should be considered a defense to aggressive state escheatment.[12]

9. *See* Andrew Hartlage, Commentary, *Unclaimed Financial Assets and the Promotion of Microfinance*, 109 MICH. L. REV. FIRST IMPRESSIONS 99, 100-101 (2011) (highlighting how different states use unclaimed property to fund programs); *see also* Azure Ltd. v. I-Flow Corp., 210 P.3d 1110, 1111 (Cal. 2009) (noting state enjoys use and benefit of funds it receives as unclaimed property). *See generally* MICHAEL A. STEGMAN & AARON MCKETHAN, CTR. FOR CMTY. CAPITALISM, UNIV. OF N.C. AT CHAPEL HILL, ESCHEATS FUNDS: AN OVERLOOKED SOURCE OF PUBLIC CAPITAL FOR BUSINESS DEVELOPMENT IN NORTH CAROLINA, (2005), *available at* http://www.ccc.unc.edu/documents/ccEscheats2005.pdf (examining unclaimed-property fund with focus on North Carolina). In Maine, the state treasurer moves all money in the state's unclaimed-property fund exceeding $500,000 into the general fund at least once a year. *See* ME. REV. STAT. ANN. tit. 33, § 1964(2) (2011) (highlighting Maine's unclaimed-property fund regulations). In 2011, Maine's unclaimed-property fund took in $23.9 million; in total, Maine has about $172.8 million in unclaimed property. *See Fact Sheet on Unclaimed Property*, ME. OFF. OF ST. TREASURER, http://www.maine.gov/treasurer/unclaimed_property/about/fact_sheet.html (last visited Sept. 27, 2012). The Louisiana unclaimed-property administrator also retains $500,000 to pay claims and deposits the remainder in the state's Bond Security and Redemption Fund. *See* LA. REV. STAT. ANN. § 9:165 (2011) (providing Louisiana's unclaimed-property fund requirements). During the 2008 and 2009 fiscal years, Louisiana collected over $50 million of unclaimed property. *See* Anderson, *supra* note 8 (providing Louisiana's unclaimed-property intake during 2008 and 2009). Tennessee has used some of its unclaimed-property funds to finance a health access program in rural parts of the state. *See* TENN. CODE ANN. § 66-29-121 (2012) (stipulating fund amounts deposited toward health access program).

10. *See Azure*, 210 P.3d at 1111 (noting funds held by state as unclaimed property rarely claimed). Nearly one in eight Americans is owed unclaimed property, and less than half of the unclaimed property collected each year is ever returned to owners. *See* Cutler et al., *supra* note 5, at 335 (discussing amount owed and average rate of return to owners). News outlets have focused on celebrities and business leaders who have not bothered to claim funds in the possession of a state. *See* Tom Bemis, *Jobs, Jolie and Jagger on Who's Who of Dead Money*, MARKETWATCH, Feb. 10, 2011, http://www.marketwatch.com/story/whos-who-in-dead-money-2011-02-10 (discussing high-profile individuals owed unclaimed funds by state treasuries). Among those owed: The Walt Disney Company turned over $659.01 in Angelina Jolie's name to California; Johnny Depp has $2159.06 from Porsche North America in the California treasurer's office; Aretha Franklin can claim $9000; and Steve Jobs had $590 waiting to be claimed, including $37.91 that was turned over by Apple, Inc. while Mr. Jobs was still living. *Id.*

11. *See generally* Am. Express Travel Related Servs. Co. v. Hollenbach, 630 F. Supp. 2d 757 (E.D. Ky. 2009), *vacated sub nom.* Am. Express Travel Related Servs. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011) (focusing on constitutionality of using unclaimed-property law changes to generate state revenue). The case focuses on the constitutionality of using unclaimed-property law changes that seek to generate additional revenue for a state. *Id.*

12. *See Hollenbach*, 630 F. Supp. 2d at 760-65, *vacated sub nom.* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011). Although not directly addressed in this Note, the underlying owners of unclaimed funds may also have due-process concerns when states rush to liquidate property such as stocks or safety-deposit-box contents through sale. *See* Taylor v. Westly, 488 F.3d 1197, 1201 (9th Cir. 2007) (holding California's unclaimed-property scheme violated due process and caused irreparable harm to owners). The Ninth Circuit held that merely publishing advertisements in newspapers announcing that the reader may

This Note will focus on the constitutional concerns raised by two specific techniques employed by states that have resulted in the escheatment of large quantities of unclaimed property: the use of contract auditors paid on a contingency basis to make unclaimed-property assessments against holders, and state and auditor reliance on statistical modeling and estimates to make assessments against holders when their unclaimed-property records are deemed incomplete or inadequate.[13] This Note will begin by explaining the history and development of escheat law, from its common-law origins in England to its modern evolution in the United States.[14] Particular attention will be paid to cases that have attempted to address issues relating to audit techniques and revenue-raising statutes.[15] Finally, this Note will introduce new considerations and propose new procedures that legislatures, courts, and state unclaimed-property administrators should heed to address procedural shortfalls in constitutionality and fairness.[16]

II. HISTORY

A. The Origins of Escheating Unclaimed Property

The common-law concept of escheatment has its origins in feudal England, where its application was limited to real property.[17] This concept eventually developed into the notion of *bona vacantia*, whereby the sovereign could claim personal property as a custodian for the rightful owner.[18] After early American colonists broke off from the Crown, the newly-formed federal government did not assert similar claims to escheat property.[19] Nonetheless, the individual

have unclaimed funds possessed by the state did not suffice as proper notice. *Id.*

13. *See infra* Part II.C.1. (discussing use of contract auditors); *infra* Part II.C.2. (discussing use of estimates and modeling). In recent years, states have increased their dependence on auditing to escheat unclaimed property. *See* Saltzman, *supra* note 5, at 1605 & n.46 (noting state use of auditors resulted in greater one-year collection than previous four combined).

14. *See infra* Part II.A. (discussing history of escheat law).

15. *See infra* Part II.C. (discussing aggressive escheat tactics).

16. *See infra* Part III.

17. *See* John V. Orth, *Escheat: Is the State the Last Heir?*, 13 GREEN BAG 2D 73, 74 (2009). When estates were granted to vassals, the sovereign retained an overlordship that entitled him and his successors to the land when those estates came to an end, whether through the death of the life tenant in the case of life estates or through death without an heir or valid will in the case of fee simple estates. *Id.*; *see also History and Evolution of Current Unclaimed Property Law*, State Tax Portfolios: Other Taxes (BNA) § 1600.02 (discussing history of unclaimed-property law).

18. *See* John A. Biek, *Jurisdictional Limitations on State Claims to Abandoned Property*, 5 ST. & LOC. TAX L. 1, 1 (2000) (reviewing history of common-law escheat). The theory behind *bona vacantia* was that the sovereign had a more equitable claim to the property than the holder did. *Id.* Under English common law, *bona vacantia* applied to personal property without an owner, not to property with an unknown owner. *See History and Evolution of Current Unclaimed Property Law*, State Tax Portfolios: Other Taxes (BNA) § 1600.02.

19. *See* Orth, *supra* note 17, at 75. This is most likely because the ability to escheat was not viewed as granted to the new government based on delegation of powers principles. *Id.*

states held onto the notion that they retained an overlying title to real property.[20] Although, at common law, the ability to escheat real property derived from recognizing the sovereign's rights, in the United States the assumption of personal property under *bona vacantia* developed under the use of the states' police powers.[21]

State laws dealt solely with real-property escheatment throughout most of the nineteenth century, but by its end, some states had begun to apply escheat principles to personal property.[22] By the second half of the twentieth century some states even recognized escheatment of intangible property.[23] Several early cases upheld the constitutionality of a state's right to escheat unclaimed property.[24] While state escheatments were frequently challenged on the grounds that they deprived property owners of due process, interfered with the operations of the federal courts and government, and violated the Constitution's Contract Clause, the Supreme Court upheld state unclaimed-property schemes on multiple occasions.[25]

B. Modern Escheat Law

1. The Derivative-Rights Doctrine

In modern escheats of unclaimed property, the state does not take title, but rather acts as a perpetual custodian until a beneficial owner comes forward; in this respect, the unclaimed-property laws of all fifty-five U.S. states and territories that require unclaimed-property remittance are not considered "true" escheat statutes.[26] The principle underlying this structure is known as the

20. *Id.* at 75-76; *see also In re* O'Connor's Estate, 252 N.W. 826, 827 (Neb. 1934) ("Clearly the theory of the law in the United States, then, is that first and originally the state was the proprietor of all real property and last and ultimately will be its proprietor, and what is commonly termed ownership is in fact but tenancy . . . .").

21. *History and Evolution of Current Unclaimed Property Law*, State Tax Portfolios: Other Taxes (BNA) § 1600.02.

22. *Id.*

23. *Id.* (discussing how states began to escheat intangible property).

24. *See* Conn. Mut. Life Ins. Co. v. Moore, 333 U.S. 541, 546 (1948) ("The state may more properly be custodian and beneficiary of abandoned property than any person."); Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 252 (1944) (holding Kentucky's deposit escheat program allowed by Due Process Clause because of strict judicial proceedings); United States v. Klein, 303 U.S. 276, 281 (1938) (holding Pennsylvania's escheatment of funds paid into courts and unclaimed for seven years constitutional); Cunnius v. Reading Sch. Dist., 198 U.S. 458, 475 (1905) (upholding state statute escheating intangible personal property after seven-year abandonment under Fourteenth Amendment); Hamilton v. Brown, 161 U.S. 256, 275 (1896) (holding escheat acceptable exercise of state sovereignty for regulation of succession of property).

25. *See supra* note 24 and accompanying text (portraying Supreme Court's willingness to allow early state escheat schemes).

26. *See* UNIF. UNCLAIMED PROP. ACT, Prefatory Note (1995), 8C U.L.A. 88 (2001) ("This Act retains the custodial features of the 1954 Act and the 1981 Act. Thus, the State does not take title to unclaimed property, but takes custody only, and holds the property in perpetuity for the owner."). As evidenced by language in the 1995 Uniform Unclaimed Property Act and referenced in the Act's statement of history, earlier iterations

"derivative rights doctrine," which essentially provides that a state's rights in unclaimed property do not extend any further than the original owner's rights in the property.[27]

2. The Priority Rules

Procedurally, the unclaimed-property laws adopted by each state require holders of unclaimed property to annually report and deliver to the state any debts or obligations owed to an owner after the dormancy period has elapsed.[28] Determining which state may take custody of a holder's unclaimed property has been the focus of several Supreme Court decisions.[29] Originally the Court, when dealing with these jurisdictional issues, analyzed whether a state could appropriately assert custody over unclaimed property based on the contacts of the holder or owner to the claiming state.[30] In 1951, the Supreme Court heard

contained similar language. *Id.* Most state unclaimed-property laws are based on either the 1954, 1966, 1981, or 1995 Uniform Act. *See* Saltzman, *supra* note 5, at 1602 (discussing state adoption of uniform acts). Still, one court observed that while the Act "is not a true escheat act, it is also true that it is not purely custodial in nature." Smyth v. Carter, 845 N.E.2d 219, 223 (Ind. Ct. App. 2006). The *Smyth* court noted that, "[u]nclaimed property acts are designed to serve the dual purposes of reuniting owners with the value of unclaimed property and giving the state, rather than the holder, the benefit of the use of the unclaimed property *pending reclamation by the owner*." *Id.* at 222 (emphasis added). Thus, the escheat structure, as it has developed, gives the state the benefit of the use of unclaimed funds until the unclaimed property is returned to the owner, which happens less than fifty percent of the time. *See* Cutler et al., *supra* note 5, at 335. The policy reasons behind allowing states to use the funds are twofold: first, to better protect money and second, to prevent a windfall to the corporate holder. *See* TXO Prod. Corp. v. Okla. Corp. Comm'n, 829 P.2d 964, 972 (Okla. 1992) (concluding Oklahoma may take temporary custody of funds from corporate holders); Texas v. Liquidating Trs. of Republic Petroleum Co., 510 S.W.2d 311, 315 (Tex. 1974) (suggesting state procedures provide best protection under circumstances at issue). Finally, although some states—most notably California, Delaware, and New York—have not adopted any version of the uniform acts, they generally follow a similar escheat framework. *See* Ethan D. Millar & John L. Coalson, Jr., *The Pot of Gold at the End of the Class Action Lawsuit: Can States Claim It as Unclaimed Property?*, 70 U. PITT. L. REV. 511, 515 (2009) (discussing states' adoption of uniform acts).

27. *See* Millar & Coalson, *supra* note 26, at 516 (defining derivative-rights doctrine and its foundation in state law). The doctrine affords that a state's ability to take custody of unclaimed property derives from the rights of the original property owner. *Id.* Thus, a state should have no greater rights to the unclaimed property than the original owner. *Id.* Courts have acknowledged the derivative-rights principle and have held that the state only takes the interest of the unknown or absentee owner. *See* State v. Standard Oil Co., 74 A.2d 565, 573 (N.J. 1950), *aff'd*, 341 U.S. 428 (1951). Each state's unclaimed-property laws, therefore, are primarily designed to outline the procedures necessary to facilitate the return of unclaimed property to an owner. *See* Millar & Coalson, *supra* note 26, at 517.

28. *See* Biek, *supra* note 18, at 2 (describing nature of state unclaimed-property laws).

29. *See infra* notes 30-39 and accompanying text (discussing cases establishing rules to determine which states take custody of unclaimed property).

30. *See* Conn. Mut. Life Ins. Co. v. Moore, 333 U.S. 541, 547-49 (1948). In *Connecticut Mutual Life*, the Supreme Court upheld New York's right to take custody of unclaimed insurance-policy proceeds issued on New York residents by out-of-state insurance companies doing business in New York. *Id.* at 551. The Supreme Court engaged in a due-process analysis and determined that because the beneficiaries, not the company, abandoned the moneys, escheatment was proper to the policy beneficiaries' state of residence. *Id.* at 548-49.

Standard Oil Co. v. New Jersey,[31] in which the State of New Jersey claimed funds based on the fact that the holders—whose unclaimed dividends, wages, and unpresented checks New Jersey hoped to escheat—were incorporated in New Jersey.[32] The Supreme Court upheld New Jersey's right to escheat the funds based on the holder's incorporation in New Jersey and fulfillment of notice requirements, despite Justice Frankfurter's strong objections to awarding the property to New Jersey.[33] Their concerns were realized when the Court's decision caused several states to shorten their dormancy periods in order to be the first to claim a holder's abandoned property.[34]

In *Texas v. New Jersey*,[35] the Supreme Court fashioned a series of clear-cut rules for determining to which state unclaimed property escheats.[36] Under these "priority" rules, unclaimed property first escheats to the state of the owner's last-known address, according to the holder's records.[37] If the owner's address is unknown or located in a state that does not escheat that particular type of property, the property escheats to the state of incorporation of the holder (subject to a right by the owner or owner's state to later claim it).[38] The Supreme Court has rejected the chance to reevaluate these guidelines, despite concerns that the second rule creates a windfall to the state of incorporation.[39]

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31. 341 U.S. 428, 430-31 (1951).

32. *Id.*

33. *See id.* at 439-41, 443 (upholding New Jersey's right to escheat). Justice Frankfurter, joined by Justice Jackson, argued against the ruling by suggesting that "the constitutional rights of the several States depend on, and are terminated by, a race of diligence" among the states. *Id.* at 444 (Frankfurter, J., dissenting).

34. *See* Biek, *supra* note 18, at 5-6 (highlighting concerns regarding states shortening statutory dormancy periods following *Connecticut Mutual Life* and *Standard Oil*); *see also* Saltzman, *supra* note 5, at 1602 (describing "race to escheat" between states). Prior to the Court's decision in *Standard Oil*, dormancy periods ranged between fourteen and twenty years; by 1954, some states had shortened them to seven years. *See* Biek, *supra* note 18, at 5-6.

35. 379 U.S. 674 (1965).

36. *Id.* at 680-82 (articulating last-known address test).

37. *Id.* at 681-82. This rule was formulated to recognize that unclaimed property is an asset of the owner, not the holder, to distribute unclaimed property among the states in proportion to the commercial activities of its residents, and to avoid using more complex legal concepts such as domicile and residence. *See* Biek, *supra* note 18, at 7.

38. *See Texas*, 379 U.S. at 682. Although in theory, a corporation's principal place of business would probably have more extensive contacts with the holder than the state of incorporation, the Court adopted the alternative standard because it was easier to discern. *See* Biek, *supra* note 18, at 7. The hope was to create a "clear rule which will govern all types of intangible obligations . . . and to which all States may refer with confidence." *Texas*, 379 U.S. at 678.

39. *See* Pennsylvania v. New York, 407 U.S. 206, 211-16 (1972) (rejecting plea that state where money orders purchased allowed to escheat under primary rule); *see also* Delaware v. New York, 507 U.S. 490, 507-08 (1993) (rejecting New York's claim that secondary rule should utilize holder's state of commercial domicile). In *Delaware*, New York claimed custody of $360 million in unclaimed dividends for unknown owners being held by transfer agents, despite the fact that most of the transfer agents were incorporated in Delaware. *Delaware*, 507 U.S. at 507-08. In the United States, Delaware receives significant benefits from taking custody of unclaimed property because the state of incorporation frequently takes custody of unclaimed property, begging the question whether incorporating in Delaware actually benefits holders. *See* Chad Livengood, *Revenue Recovering to Tune of $155 Million*, NEWS J. (Wilmington, Del.), Mar. 19, 2011,

3. The Uniform Acts

Each state has been left to create its own unclaimed-property laws and regulations outlining property types qualifying as escheatable, reporting and remittance requirements for holders, dormancy periods, and the like.[40] Still, states have generally been guided by different iterations of a uniform act.[41] The 1981 Uniform Unclaimed Property Act adopted the Supreme Court's holdings by providing that if the owner's address is unknown, or he or she either resides in a state that does not claim the property or in a foreign country, the holder's state of corporate domicile has the next claim to the property.[42] Later versions of the Uniform Unclaimed Property Act expanded on the Supreme Court's priority rules by providing that if the state of corporate domicile does not claim the property and the last known address is unknown or in a state that does not claim the type of property at issue, the state where the transaction occurred that gave rise to the unclaimed property may claim it.[43] The Uniform Unclaimed Property Act also condones the auditing of holders' records to determine compliance with state unclaimed-property laws, a lengthy look-back period for state and third-party auditors, and the use of statistical sampling if the holder has inadequate records to determine the actual amount that should be escheated.[44] Under the Uniform Unclaimed Property Act, large interest and

available at http://pqasb.pqarchiver.com/delawareonline/access/2296408161.html?FMT=ABS&FMTS=ABS:FT&date=Mar+19%2C+2011&author=CHAD+LIVENGOOD&pub=The+News+Journal&edition=&startpage=n%2Fa&desc=Revenue+recovering+to+tune+of+%24155+million ("[N]ew estimate for 2012 shows revenue from abandoned property breaking the $390 million [threshold] . . . by $35 million."). From 2007 to 2010, Delaware collected nearly $1.7 billion in unclaimed property and returned less than three percent to owners. Randall Chase, *Delaware Among States Eyeing Unclaimed Property*, BUSINESSWEEK, November 24, 2010, http://www.businessweek.com/ap/financialnews/D9JMOU0O0.htm.

40. *See generally* KENDALL HOUGHTON ET AL., COUNCIL ON STATE TAXATION, IN THE NICK OF TIME? REFORMING STATE UNCLAIMED PROPERTY LAWS: ESSENTIAL GOALS AND A REVIEW OF POTENTIAL FORUMS 4 (2009), *available at* http://www.cost.org/WorkArea/DownloadAsset.aspx?id=75198 (stating lack of uniformity in state unclaimed-property laws).

41. *See* Saltzman, *supra* note 5, at 1602 (outlining history of Uniform Unclaimed Property Acts from 1954 to 1995). The 1954 Act was born out of a need to address multi-state claims to unclaimed property. *Id.* The 1981 Act codified the *Texas* priority rules and authorized uniform reporting forms and joint agreements between the states. *Id.* As mentioned, nearly all states have adopted either the 1954, 1966, 1981, or 1995 Act. *Id. But see* Millar & Coalson, *supra* note 26, at 516 (stating Delaware, New York, and California have not specifically adopted version of uniform acts).

42. UNIF. UNCLAIMED PROP. ACT § 3(4)-(5) (1981), 8C U.L.A. 189 (2001). Corporate domicile is the state of incorporation for corporations, or the state of principal place of business for an unincorporated entity. *Id.* § 1(6).

43. *Id.* § 3(6). Given the increased need for states to take custody of unclaimed property, it follows that this rule has rarely been used and has never been reviewed by a court. *See* Biek, *supra* note 18, at 9 (noting transaction rule not yet challenged in courts).

44. *See* UNIF. UNCLAIMED PROP. ACT §§ 29(b), 30(a)-(b) (1981), 8C U.L.A. 256-58 (2001) (discussing ability to audit as well as look-back period for audits); *see also* UNIF. UNCLAIMED PROP. ACT § 20(f) (1995), 8C U.L.A. 136 (2001) (discussing use of estimations if holder has inadequate records). The 1995 Act also authorizes the use of third parties to conduct audits on behalf of a state. *See* UNIF. UNCLAIMED PROP. ACT § 20(b) (1995), 8C U.L.A. 136 (2001). The look-back periods are particularly troublesome because statutes of limitations generally do not apply in this area; some states permit auditors to analyze ten to twenty years before

penalty assessments may also result from a holder's failure to comply with a state's unclaimed-property laws.[45]

C. Aggressive State Escheat Tactics

1. Audits and Auditors

The 1954 version of the Uniform Unclaimed Property Act required that before a holder of unclaimed funds could be subjected to a compliance audit, the auditing state must show that it had a reason to believe that the holder had unreported, unclaimed funds.[46] The 1981 Uniform Unclaimed Property Act, however, eliminated the "reason to believe" requirement.[47] The effect of this change gives auditors the ability to select companies for audit based solely on the *possibility* that large amounts of unclaimed property—and future state revenue—will be uncovered.[48]

To some extent, the Fourth Amendment of the United States Constitution provides some level of protection from an unreasonable audit by requiring the functional equivalent of a warrant to be issued for governmental examinations of books and records, and prohibiting broad "fishing" expeditions by state government examiners.[49] Unfortunately, although holders may, in theory, challenge the legitimacy of an unclaimed-property audit through litigation, liberal discovery laws generally make this an unfavorable and impracticable

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the expiration of the dormancy period to find property subject to the state's escheat law. *See* Cutler et al., *supra* note 5, at 337. Third-party auditors are often compensated on a contingency-fee basis, giving them great incentives to generate estimation results most favorable to the state. *See id.* Some estimation techniques have been criticized by industry insiders as statistically questionable or inappropriate for certain businesses. *Id.*

45. *See* Cutler et al., *supra* note 5, at 337 (discussing penalty assessment for holders). As of 2002, some states charged interest as high as 18% per year, fines of up to $500 per day, and penalties of up to 25% of the value of property to be escheated for being out of compliance with state unclaimed-property laws. *Id.*

46. *See* Saltzman, *supra* note 5, at 1605 (discussing 1954 Act's "reason to believe" requirement).

47. *Id.* The comment to section 30b of the 1981 Act specifically acknowledges the departure from the "reason to believe" standard. *See* UNIF. UNCLAIMED PROP. ACT § 30(b) cmt. (1981) 8C ULA § 30 (2001) (justifying abandonment of "reason to believe" requirement because "to require as prerequisite for an examination that a state has reason to believe information has been withheld *encourages litigation* and imposes an unnecessary burden on the state").

48. *See* Saltzman, *supra* note 5, at 1605 (discussing effects of eliminating "reason to believe" standard).

49. *See* Marshall v. Barlow's, Inc., 436 U.S. 307, 312-13 (1978).

> [T]he Fourth Amendment prohibition against unreasonable searches protects against warrantless intrusions during civil . . . investigations. . . . If the government intrudes on a person's property, the privacy interest suffers whether the government's motivation is to investigate violations of criminal laws or breaches of other statutory or regulatory standards.

Id.; *see also* See v. City of Seattle, 387 U.S. 541, 544-45 (1967) ("It is now settled that, when an administrative agency subpoenas corporate books or records, the Fourth Amendment requires that the subpoena be sufficiently limited in scope, relevant in purpose, and specific in directive so that compliance will not be unreasonably burdensome."); Okla. Press Publ'g Co. v. Walling, 327 U.S. 186, 196 (1946) (quashing administrative subpoena for being overly broad).

option.[50] Additionally, because businesses often hold property that is reportable to several different states, auditors often search for unclaimed property on behalf of many states at once: a so-called "multijurisdictional audit."[51] In 1978, the Supreme Court upheld multijurisdictional audits in the tax arena with its decision in *United States Steel v. Multistate Tax Commission*.[52]

Even if the legitimacy of the audit is rarely challenged, who conducts the audit is another concern. While the 1981 and 1995 Acts permitted the use of contract firm auditors, the Acts were silent as to how auditors should be compensated.[53] A 2009 study by the Council on State Taxation found that all states permitted to engage contract-auditing firms either compensated those auditors on a contingency basis or have the statutory authority to do so.[54]

50. *See* United States v. Alabama, 434 F. Supp. 64, 64-68 (M.D. Ala. 1977) (finding liberal discovery rules apply once lawsuit has commenced). Once an assessment or escheat has been made, a holder's recourse against the state may be even more limited. *See Ex Parte* Young, 209 U.S. 123, 148 (1908) (holding Eleventh Amendment bars suits against states for damages). Only a few states provide a predeprivation or postdeprivation process to challenge unclaimed-property assessments. *See* Scott D. Smith, *Delaware and Unclaimed Property: One State's Aggressive Revenue Pursuit and How Targeted Businesses Can Respond*, 3 n.4, (Wash. Legal Found., Critical Legal Issues: Working Paper Series, Paper No. 171, 2010), *available at* http://www.wlf.org/Upload/legalstudies/workingpaper/ScottSmithWP.pdf. *But see* ARIZ. REV. STAT. ANN. § 44-338 (2012) (providing administrative appeal to challenge unclaimed-property assessments prior to delivery to state). However, the Supreme Court has held that due process requires procedural safeguards. *See* McKesson Corp. v. Div. of Alcoholic Beverages & Tobacco, 496 U.S. 18, 36 (1990) ("State[s] must provide procedural safeguards against unlawful exactions in order to satisfy the commands of the Due Process Clause."). In the tax arena, states are required to provide predeprivation procedures to challenge assessments before payment or postdeprivation processes such as refund suits. *Id.* at 39; *see also* Mathews v. Eldridge, 424 U.S. 319, 335 (1976) (determining if administrative procedures constitutionally sufficient in case regarding termination of social security benefits).

51. *See* Saltzman, *supra* note 5, at 1600 (describing multijurisdictional audits). After being contacted by an auditor working on behalf of one state, other states may be inclined to audit a holder even if they would not have otherwise. *Id.*

52. 434 U.S. 452 (1978); *see also* Kinnear v. Hertz Corp., 545 P.2d 1186 (Wash. 1976). *Kinnear* largely dealt with whether or not a multistate-tax audit violated the Compact Clause of the Constitution. *See Kinnear*, 545 P.2d at 1189.

53. *See supra* note 44 (discussing provisions of Uniform Act permitting use of contract auditors); *see also* HOUGHTON ET AL., *supra* note 40, at 9 (stating Act silent as to whether contract firms can be paid on contingency basis). Some states have been so brash as to prohibit the use of contingency-fee auditors in some instances (as in a tax audit) while still allowing it in the unclaimed-property field. *See* ARIZ. REV. STAT. ANN. § 42-6002 (2012). Paying auditors by contingency fees gives assurance to the state that the cost of the auditor's contract will not exceed the revenues produced by the audit. *See Constitutional Aspects of Unclaimed Property Acts and Their Enforcement*, State Tax Portfolios: Other Taxes (BNA) § 1600.05.

54. *See* HOUGHTON ET AL., *supra* note 40, at 8-9 (discussing states' approach to contingency auditors). After this study, North Carolina enacted legislation banning the use of contingency-fee auditors. *See* Tax Assessments—Audits and Auditors—Compensation and Salaries, 2012 N.C. Sess. Laws 152. That the auditor may be a third party is less contentious than the fee arrangement. *See* Gen. Motors Corp. v. State Tax Comm'n, 504 N.W.2d 10, 12 (Mich. Ct. App. 1993) (authorizing use of third-party auditors); *see also infra* notes 61-65 and accompanying text (describing court holdings regarding state tax auditing compensation schemes). A Maryland court described the contingency process as follows:

> The [unclaimed-property] [a]dministrator has limited resources available with which to conduct

While not directly addressing contingency-fee audits, the Supreme Court has held that a procedure, even if legislatively authorized, imposing fines by an individual having a direct financial interest in the money collected constitutes a denial of due process.[55] The Due Process Clause requires neutrality and fairness in such assessments.[56]

Despite apparently clear guidance from the Supreme Court, state courts have generally split on the legality of contingency-fee-auditing programs when directly challenged.[57] In one instance, the Georgia Supreme Court voided a state tax audit where auditors were paid on a contingency-fee basis as contrary to public policy.[58] The North Carolina Supreme Court, in contrast, held a

> the examinations of records of holders of abandoned property. Consequently, the [a]dministrator has a contract with several private vendors . . . to conduct the reviews of selected unclaimed property records. The determination to utilize the services of [the auditor] is made based on the volume of the records, the scope of the corporation's business[,] . . . any information regarding the corporation that [the auditor] may already have obtained, the number of corporate employees, shareholders and subsidiaries, and the corporation's prior reporting history.
>
> [The auditor] is paid a fee for its services equal to a percentage of the amount of abandoned property actually remitted to the Comptroller as a result of its review. [The auditor] is not paid anything for identifying property as abandoned, unless that property is in fact remitted to the Comptroller.

Comptroller of Treasury v. PHH Corp., 717 A.2d 950, 952 (Md. Ct. Spec. App. 1998) (discussing role of contingency fee auditors and their compensation arrangements).

55. *See* Tumey v. Ohio, 273 U.S. 510, 532 (1926) (holding every procedure tempting judge to forget required burden of proof denies due process). In the *Tumey* ruling, it did not matter that the individual was a member of the executive branch or that the amount may be "so small that it is not to be regarded as likely to influence improperly a judicial officer in the discharge of his duty, or as prejudicing the defendant in securing justice . . . ." *Id*. at 524. The Court noted that: "There was at the common law the greatest sensitiveness over the existence of any pecuniary interest, however small or infinitesimal, in the justices of the peace." *Id.* at 525. Such an arrangement may only be upheld where the "[i]nterest is so remote, trifling, and insignificant that it may fairly be supposed to be incapable of affecting the judgment of or of influencing the conduct of an individual." *Id.* at 531 (internal citations omitted).

56. *See* Marshall v. Jerrico, Inc., 446 U.S. 238, 242 (1980). In *Jerrico*, Justice Marshall observed:

> This requirement of neutrality in adjudicative proceedings safeguards the two central concerns of procedural due process, the prevention of unjustified or mistaken deprivations and the promotion of participation and dialogue by affected individuals in the decisionmaking process. The neutrality requirement helps to guarantee that life, liberty, or property will not be taken on the basis of an erroneous or distorted conception of the facts or the law. At the same time, it preserves both the appearance and reality of fairness . . . by ensuring that no person will be deprived of his interests in the absence of a proceeding in which he may present his case with assurance that the arbiter is not predisposed to find against him.

Id. (internal citations omitted).

57. *Compare* Sears, Roebuck & Co. v. Parsons, 401 S.E.2d 4, 5 (Ga. 1991) (holding improper tax audits with auditors paid on a contingency-fee basis), *and* Murphy v. Swanson, 198 N.W. 116, 120 (N.D. 1924) (holding contingent-fee contracts against public policy), *with* Jackson Lumber Co. v. McCrimmon, 164 F. 759, 765 (N.D. Fla. 1908) (finding contingent-fee audits not against general public policy considerations), Simpson v. Silver Bow Cnty., 285 P. 195, 201 (Mont. 1930) (finding contingent-fee audits do not violate public policy concerns), *and In re* Philip Morris U.S.A., 436 S.E.2d 828, 831 (N.C. 1993) (authorizing similar scheme).

58. *See Sears, Roebuck & Co.*, 401 S.E.2d at 5 ("The people's entitlement to fair and impartial tax

similar scheme to be perfectly legal.[59] But state courts analyzing contingency-fee-audit schemes have generally focused on public-policy arguments and have failed to address procedural due-process concerns.[60]

2. Estimation

The 1981 and 1995 Acts authorize the use of estimation and statistical sampling techniques to determine amounts that should be escheated if a holder fails to maintain adequate and accurate records.[61] Some states have also expressly approved the use of such statistical sampling by statute.[62] However, a substantive-due-process concern arises with estimation techniques when their primary motivation is to raise revenue for the state, not to reunite owners with their property.[63]

In *American Express Travel Related Services Co. v. Hollenbach*,[64] American Express challenged the legitimacy of an amendment to Kentucky's unclaimed-property law on the grounds that it could not pass rational-basis review under the Due Process Clause of the Fourteenth Amendment.[65] In granting American

assessments lies at the heart of our system . . . . Fairness and impartiality are threatened where a private organization has a financial stake in the amount of tax collected as a result of the assessment it recommends.").

59. *See Philip Morris U.S.A.*, 436 S.E.2d at 831 (noting legislature had not specifically barred fee arrangement). However, the North Carolina Court of Appeals affirmed a Property Tax Commission ruling that a contingency-fee audit "so offended conventional standards requiring fair, impartial, and uniform treatment of this State's taxpayers that [the arrangement] could not stand." *See In re* Phillip Morris U.S.A., 424 S.E.2d 222, 224 (N.C. Ct. App. 1993).

60. *See* Suburban Cable TV Co. v. City of Chester, 685 A.2d 616, 619-20 (Pa. Commw. Ct. 1996) (finding arrangement did not violate tenets of sound public policy). One case is often thought of as addressing the impartiality and lack of fairness in contingency fee audits, but the court stressed that the "investigators" were not auditors because they lacked access to taxpayer records and therefore did not fall in that category. *See* Union Pac. Res. Co. v. State, 839 P.2d 356, 380 (Wyo. 1992). Finally, in *Hubbell, Inc. v. City of Bridgeport*, the Connecticut Supreme Court noted that although the trial court wrote an extensive footnote questioning the constitutionality under due process of a contingency-fee-audit program, it would "neither reject nor endorse the trial court's dicta" on the issue. 692 A.2d 765, 770 (Conn. 1997).

61. *See* UNIF. UNCLAIMED PROP. ACT § 30(e) (1981), 8C U.L.A. 258 (2001); UNIF. UNCLAIMED PROP. ACT § 20(f) (1995), 8C U.L.A. 136 (2001).

62. *See* State v. Chubb Corp., 570 A.2d 1313, 1317 (N.J. 1989) (permitting estimations in escheat case and emphasizing reliability of extrapolation methodology). It is worth noting that even though estimation techniques are utilized when an unclaimed-property holder has inadequate or insufficient records to accurately determine an amount that should be escheated, the use of estimation rarely relates to a state's record retention requirements, which some states do not even have. *See* Smith, *supra* note 50, at 8 (describing Delaware's nonexistent records retention requirement but long look-back period for audits).

63. *See* Am. Express Travel Related Servs. Co. v. Hollenbach, 630 F. Supp. 2d 757 (E.D. Ky. 2009), *vacated sub nom.* Am. Express Travel Related Servs. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011). *McKesson Corp. v. Cook* outlines how estimations generate large amounts of revenue quickly because the liability of the holder, McKesson Corporation, ballooned from an acknowledged amount of $19,337 to $4.5 million after Delaware applied its error rate to the years under review. *See* Verified Complaint for Equitable, Declaratory, Injunctive & Other Relief, McKesson Corp. v. Cook, No. 4920 (Del. Ch. 2009), *available at* http://www.reedsmith.com/files/Uploads/Documents/McKesson.pdf.

64. 630 F. Supp. 2d 757 (E.D. Ky. 2009).

65. *Id.*

Express's motion for summary judgment, the district court stated that the statute's goal was to raise revenue, not reunite owners with their property—an independently insufficient ground to justify upholding the statute.[66] The Sixth Circuit Court of Appeals disagreed, however, and vacated the district court's decision, noting that the statute was rationally related to facilitating the state's interest in taking custody of unclaimed property.[67]

A key issue in determining the level of due process owed to unclaimed-property holders under pressure from revenue-raising state statutes is the determination of whether escheat is a "tax."[68] By definition, many escheat laws would appear to qualify as taxes.[69] Nevertheless, courts have avoided classifying unclaimed-property laws as a tax, partially because they are more akin to—and historically have been—consumer-protection measures.[70] Still, commentators have noted that when their primary purpose is to generate revenue, these statutes may cross a fine line.[71]

The Supreme Court has also determined whether or not a holder had a property interest in the property being claimed by the state, resolving the issue by establishing that where an unclaimed-property holder is a "debtor" for all intents and purposes, it is nearly impossible to establish a constitutionally protected property interest in escheatable property.[72] However, whether a holder can be established as a debtor by estimation is questionable because it is

66. *Id.* In an opinion denying the state's motion to alter, amend, or vacate the judgment, the district court observed that the statute at issue "was not enacted to further a 'legitimate' state interest. Instead, it was enacted to raise revenue for the state." Am. Express Travel Related Servs. Co. v. Hollenbach, No.3: 08-58-DCR, 2009 WL 2382407, at *1 (E.D. Ky. July 30, 2009).

67. Am. Express. Travel Related Servs. Co. v. Kentucky, 641 F.3d 685, 694-95 (6th Cir. 2011). The opinion can be read to provide two potential reasons for upholding the statute: first, that the state has a general interest in taking possession of unclaimed property; and second, that revenue raising is also a government interest that facilitates satisfaction of due-process objectives. *Id.* at 692. Other commentators have attempted to dissect (and justify) the Sixth Circuit's decision. *See* Gregory, *supra* note 7, at 326-27 (justifying state's interest and due-process rationales).

68. *See* Gregory, *supra* note 7, at 328 (underscoring importance of distinguishing unclaimed-property and tax laws for due-process reasons). The label of an assessment is not dispositive of whether the assessment may be considered a tax, which requires a more substantive analysis. *See* United States v. U.S. Shoe Corp., 523 U.S. 360, 367 (1998) (quoting Pace v. Burgess, 92 U.S. 372, 376 (1876)) (holding name alone insufficient to define tax).

69. *See* BLACK'S LAW DICTIONARY 1594 (9th ed. 2009) (defining tax as charge "imposed by the government on persons, entities, transactions, or property to yield public revenue").

70. *See* Am. Petrofina Co. of Tex. v. Nance, 859 F.2d 840, 841 (10th Cir. 1988) (criticizing defendant's characterization of unclaimed property as tax).

71. *See* Suellen M. Wolfe, *Escheat and the Concept of Apportionment: A Bright Line Test to Slice a Shadow*, 27 ARIZ. ST. L.J. 173, 176 (1995) ("When a state raises revenue from intangible property, no principled reason exists to distinguish due process requirements because the form of raising revenue is labeled tax or escheat."). To pass constitutional muster, taxes must meet nexus and proportionality requirements between the taxable activity and the assessing state. *See* Moorman Mfg. Co. v. Bair, 437 U.S. 267, 273 (1978); Am. Oil Co. v. Neill, 380 U.S. 451, 458 (1965).

72. *See* Anderson Nat'l Bank v. Luckett, 321 U.S. 233, 241-42 (1944) (substituting state for bank as debtor of depositors).

not fully and readily ascertainable that the estimated quantities of property were actually abandoned.[73] A recent decision at the state level held that holders should have protected property interests in their funds if: those funds would satisfy an unclaimed-property estimate, the holders have not affirmatively been shown to be debtors, and the underlying property has not been fully shown to be abandoned.[74] Furthermore, a determination of what constitutes a protected property interest varies between circuits, resulting in no bright-line test that clearly establishes when an interest worthy of due-process consideration arises.[75]

III. ANALYSIS

States in need of cash have discovered unclaimed property as a treasure trove to help make up lost revenue.[76] Due to a combination of the relative infrequency of owners coming forward to claim escheated property and the limited jurisprudence of auditing practices and procedures, states and their auditors have been able to move relatively unchecked in this area.[77] Nevertheless, practices such as contingency-fee arrangements and estimations should be reexamined by courts as they are both procedural and substantive deprivations of due process.[78]

A. Contingency-Fee Auditing Arrangements

As previously mentioned, third party auditors, who are often compensated by contingency fees, frequently conduct unclaimed-property audits on behalf of states.[79] The 1981 and 1995 Uniform Acts specifically included language to foster cooperation agreements between the states in unclaimed-property audits, most likely because the unique priority rules relating to unclaimed property dictate that it may flow to different states.[80] However, the current use of

73. *See* Delaware v. New York, 507 U.S. 490, 500-05 (1993) (defining key terms). In *Delaware*, the Court went to great lengths to appropriately identify the "debt," "debtor," and "creditor" in an unclaimed-property transaction. *Id.* The Court held that banks, brokers, and other depositories of unclaimed securities were the "debtors" because they were obligated to return the unclaimed securities to *identifiable* owners. *Id*.

74. *See* Am. Express Travel Related Servs. Co. v. Hollenbach, 630 F. Supp. 2d 757, 761-62 (E.D. Ky. 2009), *vacated sub nom.* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011); *see also supra* notes 66-67 and accompanying text (discussing *American Express* case).

75. *See* Gregory, *supra* note 7, at 332-36 (discussing three various "property interest theories"). Gregory concludes that simply determining a holder has no interest is not always clear and does not always extinguish a due-process claim. *Id.* at 332-37.

76. *See supra* notes 2-4 and accompanying text (discussing need of states to generate additional revenue).

77. *See supra* note 8 and accompanying text (discussing infrequency of owners claiming property); *supra* notes 46–60 and accompanying text (discussing relatively few cases dealing with aggressive auditing techniques).

78. *See supra* notes 54–60 and accompanying text (discussing contingency fee arrangement and estimation opinions by various courts).

79. *See supra* notes 51-52 (discussing authorization of use of contract auditors and reasons for their use).

80. *See supra* notes 30-39 and accompanying text (outlining Supreme Court's priority rules for

multijurisdictional audits adds to a predatory auditing environment by third-party auditors.[81]

When tasked with an audit for one state, private auditing companies then solicit other states, seeking authority to act as their agent to audit an unclaimed-property holder as well.[82] States have a bevy of reasons to accept the auditor's offer: their statutes may not require that any formal selection criteria be met before an audit takes place, the auditor is likely compensated by a percentage of the unclaimed property recovered so the state will not suffer any loss by engaging the auditor, and states are strapped for cash so the property recovered will likely be usable revenue because it is rarely claimed by owners.[83] The 1981 and 1995 Uniform Acts do not require that a "reason to believe" standard must be met before allowing an unclaimed-property audit.[84] Because states may easily authorize audits and auditors can pick potential targets by hawking their services from state to state, suspected holders are sometimes chosen for an audit based on no more than the scant possibility that unclaimed property will be recovered.[85] Meanwhile, companies under audit expend significant amounts of time and money defending themselves in the audit process.[86]

Having no identifiable, formal criteria to trigger an audit could raise constitutional issues as well: The Fourth Amendment generally provides that the search of private property without consent is unreasonable unless authorized by a valid search warrant.[87] A formal warrant can be discarded if

determining which state gets benefits of unclaimed property); *see also* UNIF. UNCLAIMED PROP. ACT § 23 (1995), 8C U.L.A. 141 (2001) (authorizing joint agreements and adopting uniform reporting forms); UNIF. UNCLAIMED PROP. ACT § 33 (1981), 8C U.L.A. 262 (2001) (same).

81. *See* Saltzman, *supra* note 5, at 1605 (describing how auditors work with various states).

82. *Id.*

83. *See supra* notes 46-48 and accompanying text (noting deletion of "reason to believe" standard from later versions of uniform acts); *supra* notes 53-54 and accompanying text (discussing how contingency-fee systems work); *supra* notes 2-4 and accompanying text (describing financial perils of states); *supra* note 8 and accompanying text (describing infrequency of owners claiming their property).

84. *See supra* note 47 and accompanying text (discussing elimination of "reason to believe" standard and reasons for its removal).

85. *See* Saltzman, *supra* note 5, at 1605 (describing roles of auditors in picking targets where no formal selection criteria required).

86. *See* HOUGHTON ET AL., *supra* note 40, at 17. One holder remarked:

> The initial scope of a Delaware audit is . . . massive . . . . Due to the aggressive nature of the contingent fee auditor and the State, it is a necessity to retain outside legal counsel and outside advisors to assist. To date our company has spent in excess of $800,000 in fees to defend the audit and there is still substantial work left to do.

Id. (internal quotations omitted). Another audit victim remarked that "[t]he audit process is time consuming and costly. Audit[s] last[] 2-5 years on average. Requests for records from archived computer systems require costly computer support to retrieve." *Id.* (internal quotations omitted).

87. *See* Camara v. Mun. Court of S.F., 387 U.S. 523, 528-29 (1967) (noting searches presumptively unreasonable absent search warrant or consent). Common events triggering state audits include: failing to report unclaimed property for several years or failing to ever report to a state, submitting so-called "negative"

the enforcement procedures contained in a relevant statute are roughly equivalent to those contained in a formal warrant and provide a mechanism for courts to enforce the search.[88] One potential reading of a 1978 Supreme Court case, *Marshall v. Barlow's, Inc.*,[89] would require an inquiry during any administrative examination to investigate how an agency decided to initiate a particular search.[90] Therefore, states adopting unclaimed-property laws lacking a "reason to believe" standard potentially violate the Fourth Amendment's requirements, and states relying on those provisions to conduct audits may be in violation as well.[91]

As the unclaimed-property scheme exists now, auditors act as bounty hunters by examining books and records with little or no incentive to investigate with fairness or impartiality because their fees are paid as a percentage of their findings.[92] While at least one court has ruled that an auditor compensated by contingency fees violates public policy, other courts have decided exactly the opposite, or have not had the opportunity to make a determination.[93] The Supreme Court crafted language in a prohibition-era opinion that addressed the imposition of penalties by a government actor with a direct interest in the outcome and held that such schemes are due-process violations, largely because the requirement for fairness and impartiality cannot be met.[94] While unclaimed property generally does not "belong" to the holder, it is not "unclaimed" until a final decision has been rendered; even so, a holder can be thought of as a trustee or bailee with limited property interests, but interests nonetheless.[95]

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reports indicating there is no unclaimed property to report, failing to report types of property common in the particular holder's industry, and reporting amounts inconsistent with industry expectations. *See* Saltzman, *supra* note 5, at 1604.

88. *See* Marshall v. Barlow's, Inc., 436 U.S. 307, 323 (1978) (noting warrant requirement "provide[s] assurances from a neutral officer that the inspection is reasonable under the Constitution").

89. 436 U.S. 307 (1978). In *Marshall*, the Court ruled that Occupational Safety and Health Act of 1970 (OSHA) agent searches without a warrant or the equivalent were unconstitutional. *Id.* at 325.

90. *See* Saltzman, *supra* note 5, at 1607 (identifying possible readings of *Marshall*).

91. *Id.* Specifically, the Fifth Circuit ruled that a "search will be reasonable if it is based either on (1) specific evidence of an existing violation, (2) a showing that reasonable legislative or administrative standards for conducting an inspection are satisfied with respect to a particular establishment, or (3) a showing that the search is pursuant to an administrative plan containing specific *neutral* criteria." *See* Miss. Power v. New Orleans Pub. Serv., 638 F.2d 899, 907-08 (5th Cir. 1981) (emphasis added) (internal citations and quotation marks omitted).

92. *See* Saltzman, *supra* note 5, at 1607 (suggesting current escheat system never challenged).

93. *See* Sears, Roebuck & Co. v. Parsons, 401 S.E.2d 4, 5 (Ga. 1991) (holding contingency-fee auditing violates sound public policy). *But see In re* Phillip Morris U.S.A., 436 S.E.2d 828, 831 (N.C. 1993) (upholding contingency fee contracts). *See generally supra* notes 57-60 and accompanying text (discussing cases dealing with contingency-fee arrangements).

94. *See* Tumey v. Ohio, 273 U.S. 510, 523 (1927) ("[I]t certainly violates the Fourteenth Amendment and deprives a defendant . . . of due process of law to subject his liberty or property to the judgment of a court, the judge of which has a direct, personal, substantial pecuniary interest in reaching a conclusion against him in his case.").

95. *See* Saltzman, *supra* note 5, at 1614 (discussing rights of holders in unclaimed property); *see also*

B. Estimation

Although many states do not require holders to retain unclaimed-property records for a specific period of time, holders under audit are routinely subjected to statistical models and estimation techniques to determine amounts due to a state when the records to determine escheat compliance are unavailable or deemed inadequate.[96] A hesitation to allow estimations is not novel in the unclaimed-property arena: In early escheat cases, the Supreme Court specifically rejected the arguments of New York and Pennsylvania that an owner's last known address could be determined using statistical sampling.[97] Nonetheless, today such techniques are employed when holders lack adequate records to accurately determine amounts of property that may be subject to escheat.[98]

In *Delaware v. New York*,[99] the Supreme Court noted that describing the parties as debtors and creditors in the unclaimed-property context was legally significant because the state's power to escheat is based on the "law that creates property and binds persons to honor property rights."[100] An estimation, on the contrary, creates abandoned property—although it is not characterized as such under the property law—and the holder has not yet been established as a debtor.[101] Therefore, it is unclear whether estimation creates the substantial belief of abandonment that due process requires.[102] Furthermore, the Supreme Court has specifically ruled that not only must states provide safeguards against unlawful exactions, but whether those safeguards are constitutionally adequate depends on a balance of the private interest, the government's interest, and the

supra notes 72-75 and accompanying text (discussing jurisprudence regarding determinations of whether holder has property interest in escheatable property).

96. *See supra* note 62 and accompanying text (outlining lax or nonexistent state record retention requirements).

97. *See* Delaware v. New York, 507 U.S. 490, 508-09 (1993) (acknowledging no jurisdictional argument for allowing statistical showing of creditors' addresses). The Court in *Pennsylvania v. New York* rejected an identical argument to use estimations to identify owners' addresses. *See* 407 U.S. 206, 219-20 (1972).

98. *See supra* note 61 (citing sections of 1981 and 1995 Uniform Unclaimed Property Act authorizing use of estimates). In some instances, holder records can be inadequate because no statute of limitations defense is afforded a holder who has not filed unclaimed-property reports; for example, in Delaware an audit could look back as far as 1981 (the year Delaware's unclaimed-property law was established). *See* DEL. CODE ANN. tit. 12, § 1158(a) (2012). The statute provides a three-year audit time frame for a holder who has filed a report, and six years are afforded if there is a greater than twenty-five percent omission. *Id.* Some states are even less forgiving, such as California, Connecticut, Georgia, New York, Ohio, and Texas, all of which provide no statute of limitations for an audit look-back period, even if reports were filed. *See* Smith, *supra* note 50, at 2-3 n.3.

99. 507 U.S. 490 (1993).

100. *Id.* at 501. The Court also noted that the "law that creates property necessarily defines the legal relationships under which certain parties ('debtors') must discharge obligations to others ('creditors')." *Id.* at 502.

101. Smith, *supra* note 50, at 10.

102. *Id.*; see Anderson Nat'l Bank v Luckett, 321 U.S. 233, 240 (1944) (stating Kentucky's escheat statute only applicable to abandoned property).

risk of an erroneous deprivation of the interest through current procedures as well as the probable value of additional or substitute procedures.[103]

A strong argument against estimation goes back to the derivative-rights doctrine, which holds that a state's right to take unclaimed property derives from the rights of the missing owner.[104] It is true, however, that one purpose of the unclaimed-property laws is to give the state the benefit of the use of unclaimed property until it is claimed.[105] This does not mean, however, that an acceptable purpose of the unclaimed-property laws is to generate revenue for the state.[106] The derivative-rights doctrine further compels that in order for intangible property to be escheatable, a holder must have a fixed and certain obligation to pay on the property.[107] When escheating funds, a state merely acts as a "conservator" of the property, rather than a primary party with a claim to the property.[108] When money and property is escheated through an estimation, the state does not stand in the shoes of any owner because the escheated funds and property are not attributable to anyone; the logical conclusion, therefore, is that the calculation of these amounts is driven by revenue-raising motivations, which alone produces further due-process concerns.[109]

States have used unclaimed-property laws to raise revenue by aggressively estimating a holder's liability when the auditing entity determines a holder's own records are inadequate to determine unclaimed-property liability that is attributable to an underlying owner.[110] Unclaimed-property laws with the primary purpose of raising revenue were recently challenged in *American*

103. *See* McKesson Corp. v. Div. of Alcoholic Beverage & Tobacco, 496 U.S. 18, 36 (1990) (declaring states must provide safeguards against unlawful property exactions); Mathews v. Eldridge, 424 U.S. 319, 335 (1976) (stating factors for determining constitutionality of safeguards).

104. *See supra* note 27 and accompanying text (discussing derivative-rights doctrine).

105. *See supra* note 24 and accompanying text (discussing states' ability to benefit from unclaimed property).

106. *See* Am. Express Travel Related Servs. Co. v. Hollenbach, 630 F. Supp. 2d 757, 764 (E.D. Ky. 2009), *vacated sub nom.* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011) ("Because it is clear that the state's objective was to raise revenue rather than to reunite citizens with lost property, [the statute which shortened the abandonment period for checks] does not satisfy rational basis review.").

107. *See* Millar & Coalson, *supra* note 26, at 520 (stating holder must have an "unqualified" and "liquidated" obligation to pay on property). Generally the state must prove this fact. *See id.* at 520 n.22. In this sense, the holder is a "debtor" with no interest in the funds. *See* Delaware v. New York, 507 U.S. 490, 502 (1993) ("Funds held by a debtor become subject to escheat because the debtor has no interest in the funds . . . .").

108. *See* Conn. Mut. Life Ins. Co. v. Moore, 333 U.S. 541, 547 (1948) ("The state is acting as a conservator, not as a party to a contract.").

109. *See supra* note 62 (noting estimated amounts in escheat based on mathematical formulations and not actual holder records); *see also Hollenbach*, 630 F. Supp. 2d at 764, *vacated sub nom.* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011) (highlighting due-process concern with solely revenue-raising motivations).

110. *See supra* notes 61-63 and accompanying text (discussing unclaimed-property revenue-raising laws and aggressive estimation).

Express, although the Sixth Circuit ultimately upheld the statute in question.[111] While the appeals court's exact reasoning is ambiguous, it is possible that either interpretation of its reasoning for holding that a revenue-raising unclaimed-property law passes rational basis muster may be erroneous.[112]

The Sixth Circuit has at least partially upheld the revenue-raising Kentucky statute on the grounds that revenue generation is a legitimate state interest.[113] However, if courts accept this reasoning up front—that is, acknowledge that these statutes may serve only to raise additional revenue for a state—the designation of unclaimed-property laws as either consumer-protection mechanisms or taxes will continue to blur.[114] The key complication with a court simply acknowledging that unclaimed-property laws *do* resemble taxes arises out of the Supreme Court's priority rules, which do not require states that claim a holder's unclaimed property to meet the same standards of nexus and apportionment required when a state makes an assessment to generate tax revenue.[115] While the Supreme Court could revisit the priority rules to better coalesce with the same due-process requirements afforded in tax, as previously noted, the Supreme Court has consistently declined to alter or reconsider its established unclaimed-property priority rules.[116]

The Sixth Circuit used flawed logic when it determined that the state's interest in assuming possession of unclaimed property was sufficient to support due-process considerations.[117] Under this analysis, nearly *any* legislative modification to a state's unclaimed-property laws would satisfy rational-basis review.[118] If this reasoning were sufficient, there would be almost no due-process restrictions on state escheatment.[119]

Commentators have noted that revenue-raising escheat laws could gain support if revenue raising actually fostered the goal of owner reunification with unclaimed property.[120] Specifically, arguments have been put forth that suggest

111. *See Hollenbach*, 630 F. Supp. 2d at 757, *vacated sub nom.* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685 (6th Cir. 2011).

112. *See supra* note 67 and accompanying text (discussing Sixth Circuit's reasons for upholding Kentucky's statute).

113. *See* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d 685, 691-93 (6th Cir. 2011).

114. *See* Gregory, *supra* note 7, at 328 ("If a court accepts the proposition that unclaimed property laws are intended to 'yield public revenue,' there is no principled reason to treat these measures differently than taxes . . . ."); *see also* Wolfe, *supra* note 71, at 176 (distinguishing priority rules and subjecting states raising revenue through unclaimed property to due-process protections).

115. *See supra* notes 28-39 and accompanying text (discussing Supreme Court's priority rules authorizing states to claim unclaimed property); *supra* note 71 and accompanying text (discussing apportionment and nexus requirements of valid tax laws).

116. *See supra* note 39 and accompanying text (discussing Court's decision to avoid whether current priority rules provide state of incorporation windfall).

117. *See* Am. Express Travel Related Serv. Co. v. Kentucky, 641 F.3d at 693.

118. *See* Gregory, *supra* note 7, at 327 (arguing Sixth Circuit's potential rationale problematic).

119. *Id.* (noting highly deferential rational-basis review creates unreasonable results).

120. *Id.* at 337-44 (arguing reunification of owners and property fostered by escheat laws motivated by revenue-raising).

revenue-raising statutes foster reunification because: States are better custodians of unclaimed property than holders; owners benefit if unclaimed property is gathered in the hands of a common holder thus increasing the likelihood of claiming it; and revenue-raising laws encourage record retention by holders, arguably to avoid an estimation.[121] As to the first point, states are using unclaimed property to further their financial security, so the notion that they are better holders because of their financial position is circular and likely incorrect.[122] In the case of estimations, the support of the first and second arguments becomes even more unclear because states are not taking custody of property that anyone can actually come forward and claim.[123] Additionally, claim rates for unclaimed property are relatively low compared to the amounts that are taken in by states year after year, and no evidence suggests any correlation between reunification rates, estimation, and statistical sampling.[124] Third, a common concern among all of these justifications is that they incentivize a "race to the bottom" for states to take custody of unclaimed property by encouraging early and frequent escheatment—a concern the Supreme Court specifically addressed and aimed to avoid when it crafted the unclaimed-property priority rules.[125] Finally, if states wished to incentivize holders to retain records for a certain amount of time, the most narrowly tailored way of achieving this would be to simply create unclaimed-property record-retention requirements, which most states currently lack.[126]

IV. CONCLUSION

Unclaimed-property funds represent an extensive source of revenue for the states. As states have faced tough fiscal times, they have begun taking custody of unclaimed property through the employment of aggressive techniques in an attempt to generate nontax revenue. The cost, however, of deriving this benefit is born by unclaimed-property holders who are being subjected to costly audits and liability estimations primarily motivated by raising revenue. By utilizing unclaimed property purely as a revenue source rather than a consumer-protection mechanism, states are violating fundamental tenets of procedural and substantive due process through the use of contingency-fee auditors and

121. *Id.*

122. *See supra* note 3 and accompanying text (discussing states' dire financial situation and possible legislation allowing states to file for bankruptcy protection).

123. *See supra* note 73 and accompanying text (discussing whether estimation amounts escheatable because they do not belong to identifiable owner).

124. *See supra* note 10 and accompanying text (discussing low claimant rate of unclaimed property by states).

125. *See supra* note 33-34 and accompanying text (discussing Supreme Court's concerns with "race to escheat").

126. *See supra* note 62 (discussing lack of record-retention requirements while mandating estimations when holders lack sufficient records).

aggressive estimation techniques. As has been observed, the purpose of state unclaimed-property laws is twofold: to reunite lost owners with their property, and to give the state the benefit of the use of such property *until it is claimed*. State courts and legislatures evaluating changes to unclaimed-property laws should remain aware of how these two ideas operate in tandem by prohibiting revenue raising as a primary purpose of unclaimed law alterations and administration, and remembering the presumption that the property collected should be attributable to some beneficial owner.

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