The “door is open” for Delaware’s new unclaimed property voluntary disclosure agreement program being implemented by the Secretary of State and which differs significantly from the old VDA program, which was administered by the State Escheator. Most notably, the new program offers shortened lookback periods to holders that agree to participate by a certain date. In this article, attorneys at Alston & Bird review the new program and caution holders on the terms and conditions as well as identify some of the possible benefits.


By Alston & Bird LLP’s Unclaimed Property Practice

Introduction

On July 11, 2012, Delaware Governor Jack Markell signed Delaware Senate Bill 258 (“S.B. 258”) into law, thereby granting the Secretary of State (as opposed to the State Escheator) a limited three-year window to enter into voluntary disclosure agreements (“VDAs”) with holders of unclaimed property (the “New VDA Program”). Previously, only the State Escheator had the authority to enter into unclaimed property voluntary disclosure agreements (the “Old VDA Program”). S.B. 258 set forth a number of key provisions of the New VDA Program, including shortened look-back periods. Unlike the look-back period for the Old VDA Program, which requires holders to report property dating back to 1991, S.B. 258 provided that holders who enter the New VDA Program with the Secretary of State by June 30, 2013 and complete the VDA by June 30, 2014, will be eligible for a shortened look-back period to 1996.2 Holders who enter the New VDA Program after June 30, 2013 but before June 30, 2014, but still complete their VDA by June 30, 2015, will be eligible for a shortened look-back period to 1993. Holders may not apply for the New VDA Program after June 30, 2014.

In the roughly six months since enactment of S.B. 258, the Delaware Secretary of State has (1) selected a VDA program administrator, Drinker Biddle & Reath, LLC (the “VDA Administrator”), a Philadelphia law firm with Delaware presence, to design and administer the New VDA Program; (2) drafted Implementing Guidelines to describe with particularity the substantive methods that would be employed and the standards that would be utilized in reviewing holder VDA submissions; (3) set up a website for interested parties [http://www.delawarevda.com/] that provides access to the rel-


2 Both the Old VDA Program and the New VDA Program provide significantly shorter look-back periods than Delaware routinely applies in unclaimed property audits. In an audit, liability is typically asserted – usually through extrapolation – all the way back to 1981. Note also the recently introduced H.B. 2, which would allow a holder to qualify for the shortened look-back period to 1996 if it applied for participation by June 30, 2013 and completed the VDA process on or before June 30, 2013. See infra., note 7.

3 Secretary of State, Implementing Guidelines, Abandoned or Unclaimed Property Voluntary Disclosure Agreement Program 2012, available at http://
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In addition, the Secretary of State has engaged in a targeted outreach campaign, sending two sets of letters to what we understand to be more than 500 companies with respect to which the Secretary of State’s databases indicate a likelihood that the companies have not been in compliance with Delaware’s unclaimed property laws. In November 2012, Secretary of State Jeffrey Bullock first informed the recipients of these letters that the New VDA Program exists, and that the “door is open” to all companies that wish to register and participate. Importantly, the Secretary sent a follow-up letter in mid-January 2013 to the same group of companies (with the exception of those that had already applied to participate in the New VDA Program) that reinforces the potential risk of not responding to the Secretary’s invitation, noting that although the Division of Revenue stopped issuing unclaimed property audit notices in July 2012 (when the New VDA Program law was passed), the Division of Revenue is authorized to re-commence issuance of such audit notices after Feb. 1, 2013. Indeed, we have been advised informally that a new batch of audit notices will likely be sent out by the State Escheator/Division of Revenue in early February, providing an additional incentive for Delaware-incorporated companies that are not currently in full compliance to consider whether the New VDA Program presents an opportunity to come into compliance with the law on a more favorable basis than options that previously were available (and certainly on a more favorable basis than will be the case if the company is selected for audit).

**Essential Features of the New VDA Program**

The following are several key features of the New VDA Program, including the various phases that it entails:

- **Registration:** The holder submits a Form VDA-1 and commences the VDA process, assuming it is qualified to participate in the New VDA Program. Such qualifications include that the holder has not received a notice of audit, is not currently under audit by Delaware, and has not initiated participation in the Old VDA Program.

- **Nondisclosure Agreement and Introductory Meeting/Teleconference:** In advance of any substantive discussions, the holder should negotiate and enter a Confidentiality and Nondisclosure Agreement (“NDA”) with the VDA Administrator, which also extends to the two accounting firms with which the VDA Administrator subcontracts for purposes of reviewing VDA submissions. After the NDA is finalized and executed, the holder provides organizational information for discussion with the VDA Administrator. During the initial meeting or teleconference, the parties discuss the VDA timeline and set general expectations regarding the VDA milestones.

- **VDA Scoping and Timeline:** The holder reviews its records to determine the entities, property types, and years to be included in the scope of the VDA, and to establish years for which records are complete and searchable (i.e., not subject to extrapolations of liability). The amount of time it can take to complete this phase can range between two and three months and sometimes longer depending on the holder. The VDA Administrator will conduct monthly status meetings during the entire VDA timeline to address any issues or questions that may arise.

- **Records Review/Testing/Remediation:** The holder will identify transaction-level detail for review, testing (as appropriate), and remediation to determine an initial potential liability. Where, as in most instances, complete and searchable records do not exist for one or more property types for the entire look-back period covered by the VDA, a sample will be drawn from the “base years” established in the scoping phase, and the items included in the sample(s) will be researched to determine if they represent unreported unclaimed property. Through this process, an “error rate” of unreported property is established for each property type, to be applied to years for which complete and searchable records are not available in order to determine the projected total unclaimed property liability for such years. The timing to complete the review, testing and remediation can take three to six months, sometimes longer depending on the holder. Before testing and remediation begins, a status meeting is conducted with the VDA Administrator to agree upon methodologies and processes for the drawing of samples, and testing and remediation. This may include pre-approval by the VDA Administrator of the verbiage of any correspondence that will be utilized as customer, vendor or employee outreach in the remediation process.

- **Settlement:** The holder then presents its VDA settlement proposal and enters into a settlement agreement (Form VDA-2), which provides for property-
specific releases and indemnification. The timeline to complete this phase can be between two and four months, sometimes longer depending on the holder. Additional meetings may be conducted to address any questions and resolve open issues.

Legislation to Amend Senate Bill 258 and Increase Attractiveness of New VDA Program

House Bill 2 (“H.B. 2”) was introduced on Jan. 10, 2013 and passed the Delaware House of Representatives on Thursday, Jan. 17. The legislation would amend Section 1177, Chapter 11 of Title 12 of the Delaware Code, which contains the statute authorizing the New VDA Program as enacted by Senate Bill 258, in three potentially significant respects. They are as follows:

- Allows a holder that has applied to participate in the New VDA Program by June 30, 2013 to qualify for the shortened look-back period to 1996, provided that such holder completes the VDA and submits payment on or before June 30, 2015. As discussed above, these requirements currently must be satisfied on or before June 30, 2014 in order to receive the 1996 look-back period.
- H.B. 2 therefore provides holders that apply to participate in the New VDA Program prior to June 30, 2013 up to one additional year to enter into an agreement and make payment or enter into a payment plan. In addition to this amendment extending the time by which to finalize a VDA, the Secretary of State also has adjusted the earlier 9-month timetable (which was originally represented in the Secretary of State’s Implementing Guidelines to be strictly applicable, unless a compelling reason was provided for an extension) to complete the VDA Work Plan and submit a VDA payment. Holders and their representatives have noted to the Secretary and VDA Administrator that, although their goal is to resolve VDAs in a timely manner, many VDA submissions would require more than nine months to complete, given the fact that an unclaimed property VDA is a labor-intensive process that involves sustained cooperation among internal business groups, outside advisors and state administrators. In our discussions with the Secretary and the VDA Administrator, we have received assurances that they understand that the 9-month guideline will be insufficient in many, and perhaps most, VDAs and that during the introductory meeting, the holder, its advocate and the VDA Administrator will agree to a timeline that fits each holder, which can range from several months for some holders with limited potential liability to as long as two or more years for complex holders. The Secretary of State made clear that the fixing of a timeline is done in order to keep the VDA on track and set common expectations at the beginning of the process, and with the monthly status calls, the timeline can and will be adjusted accordingly. However, even though the 9-month period originally established as the mandatory period for completion of a New VDA has been retracted, and the original June 30, 2014 deadline for completing the VDA process and qualifying for the 1996 look-back has been extended to June 30, 2015, time still remains of the essence to obtain the benefits of the New VDA Program.
- Clarifies that a holder that has previously entered into a VDA prior to June 30, 2012 (i.e., under the Old VDA Program) may enter into the New VDA Program with respect to any related party that was not included in an earlier VDA or with respect to property types and/or periods that were not included in a prior VDA.
- Clarifies the existing duty of the State Escheator to protect confidential information by confirming that such duty covers the entirety of Chapter 11 of Title 12 of the Delaware Code (in other words, information and the fact of a VDA submission are intended to be confidential and not subject to State FOIA requests).

Additional Guidance and Feedback From the Delaware Administration Regarding Specific Aspects of VDA Filings

We are representing numerous clients currently involved in the New VDA Program submission process, and have been asked to advise other holders concerning the advisability of registering for this program. In the course of these consultations, a number of specific factual circumstances have been described that could have an impact on the VDA process and the potential outcome for a given holder.

In direct discussions with the Secretary of State and the VDA Administrator, we have broached the following issues, which may be of import to holders that have yet to reach a decision concerning the advisability of the New VDA Program:

Acquisitions Post VDA Acceptance

We understand that in circumstances where a holder has registered for the program and subsequently acquires new entities in stock purchases, whereby the holder succeeds to any outstanding unclaimed property liabilities the acquired entities may have, Delaware welcomes the expansion of the VDA scope to include acquired entities. Given the practical challenges of bringing entities into the VDA that may not have been examined closely to identify unclaimed property exposures, the VDA Administrator would work with a holder to manage the process for both the original registrants and the newly in-scope acquired entities. For instance, a two-track VDA process could be utilized so as to permit progress to be made on parallel tracks, in keeping with the holder’s different stages/states of information.

Property Type-Specific VDA

As H.B. 2 makes clear, property-specific VDAs are permitted, and in fact encouraged.

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6 The Form VDA-2 is also available on the Secretary of State’s new website. See http://delawarevda.businesscatalyst.com/forms-and-documents.
8 VDAs initiated after June 30, 2013 but before June 30, 2014 may qualify for a look-back period to 1993 if the VDA process is still completed by June 30, 2015.
Primary Purpose Not to Raise Revenue/Prospective Compliance of VDA Filers

The Secretary has represented that the primary purpose of the New VDA Program is not to raise revenue but is future annual compliance by Delaware companies. According to the Secretary, annual compliance is ultimately a more predictable revenue source, and the Secretary believes that continued reliance on unclaimed property audit revenues hurts the attractiveness of Delaware’s brand from a business formation standpoint.

Resolution of Legal Issues Associated With VDAs

One issue that the Implementing Guidelines did not make clear, and that is of concern to us, is how legal issues or disputes associated with a holder’s potential liability would be addressed and resolved. Our understanding is that all such legal issues/disputes would be handled by the VDA Administrator in consultation with the Secretary of State. The VDA Administrator is already aware of certain issues, including for example proper sampling methodology.

While estimation of liability by extrapolation was certainly a part of the Old VDA Program, the New VDA Program’s Implementing Guidelines suggest that the State and the holder will be able to agree on the estimation/extrapolation methodologies before the VDA is submitted. Under the Old VDA Program, the estimation/extrapolation methodology was often tailored to the expectations of the State Escheator, and any disagreement on methodology occurred after the VDA was submitted. As a result, holders (and their advisors) were wary to deviate from the methodologies that were known to be acceptable, even if they had supportable reasons to do so. Moreover, disagreements with respect to the methodologies employed often became a barrier to closing the VDA, and holders sometimes chose to concede the issues in order to close the VDA. Since the New VDA Program seems to permit estimation to be addressed and agreed to before the VDA is submitted, it may afford holders the ability to advocate for estimation/extrapolation methodologies that, in the past, were not employed or were only addressed at the end of the process.

Three-Year Compliance Post-VDA

In response to holders’ and representatives’ questions concerning whether perpetual compliance (i.e., filing unclaimed property reports on an annual basis) was required in order for a VDA submitted under the New VDA Program to be valid, the Secretary and VDA Administrator have revised Form VDA-2 to clarify the requirement of future compliance and the State’s ability to “void” the VDA. As originally drafted, the VDA closing agreement indicated that failure to comply with Delaware unclaimed property law at any time in the future could theoretically result in voiding the VDA. Now, the future compliance condition is limited to three years.

The administration has indicated that the three-year post-VDA compliance requirement would be monitored by the Department of Finance. We discussed with the Secretary of State and the VDA Administrator the fact that many companies, on a go-forward basis, may not have Delaware-address or foreign-address property that would be required to be reported to Delaware for one or more years. In the absence of a negative reporting requirement, we noted how difficult it would be to

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9 Implementing Guidelines, at 3.

monitor and verify future compliance. We suggested perhaps that holders could send a letter to the Secretary of State’s Office or Department of Finance documenting that the company has reviewed its records and determined it had no property to report. The Secretary of State and VDA Administrator informed us that they are aware of the issue, and that the State is considering introducing a negative reporting requirement or some other method for affirming that no property is believed to be reportable to the State for a particular year.

**Equity Audits**

While the published information, including the Implementing Guidelines, do not address the inclusion of abandoned equity interests or other securities in the New VDA Program process, the Secretary of State and VDA Administrator have indicated to us that such inclusion will be optional, at the holder’s election. If equity/securities are not included in the New VDA Program, they will not be included in the release of liability at the conclusion of the VDA process.

**Conclusion**

In light of the continuing evolution of the New VDA Program, holders should take a careful second look at its terms and conditions, as well as its potential benefits, if they previously decided that the cons outweighed the pros. Further, holders should gain a clear understanding of how their particular legal issues may be addressed within the context of the New VDA Program prior to registering, especially given the opportunity to engage the Secretary and the VDA Administrator on such issues.

We have four specific recommendations to any company that is considering whether to register for the New VDA Program. They are as follows:

- **Scope before you sign up** – understand the entities in your affiliated group that have material Delaware liabilities (presumably due to being Delaware-domiciled), as well as the relevant years and property types for each in-scope entity. Delaware is according a fair amount of discretion to holder registrants to make these determinations, but is conditioning its release from liability to only what is reported and paid over to the state.

- **Retain legal counsel and consultants** – as noted above, the process is labor-intensive, must be completed within a fairly tight timeframe (even with extensions beyond the original 9-month deadline), and many procedural and substantive legal issues must be navigated in preparation of the VDA proposal.

- **Take advantage of ready access to the Secretary of State and VDA Administrator**, but come prepared to maximize the benefit of such interactions.

- **Carefully develop and document any positions concerning holder-specific circumstances that may impact any “generally applicable” guidelines the VDA Administrator releases.**