



Unclaimed Property ADVISORY ■

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Pushing Beyond the Limit: Examining the Scope of Subpoenas Issued During Unclaimed Property Audits

On July 10, 2020, the Delaware Court of Chancery [handed a victory to AT&T](#) in quashing a subpoena issued by the Delaware Department of Finance in the course of an ongoing unclaimed property audit. Although the victory may be only temporary for AT&T, the decision may have broader and more long-standing implications for other holders undergoing Delaware unclaimed property audits.

The issuance of the department's subpoena on behalf of the State Escheator stemmed from an ongoing audit of AT&T that was initiated in 2012 (and was subsequently converted into an expedited audit under Title 12, Section 1172(c) of the Delaware Code). The department designated a third-party auditor, Kelmar Associates, to conduct the audit. Kelmar requested AT&T's records going back 20 years from the commencement of the audit to 1992 and specifically asked AT&T for information about every check AT&T issued from 27 of its accounts. In order to comply with this request, AT&T had to identify every check issued, the general ledger account to which the check was recorded, the check's disposition status, the payee name and address, and the amount of the check. AT&T initially worked with Kelmar to satisfy the information requests, but the company objected to subsequent information requests submitted by Kelmar. AT&T continued to object to the additional information requests, and after additional compliance notices submitted by Kelmar and the department went unanswered, the department terminated the expedited audit on October 31, 2019, and on November 8, 2019 issued an administrative subpoena seeking the production of these documents.

In response to the subpoena, AT&T filed an action in federal court contending that terminating the expedited audit and serving the subpoena violated AT&T's Fourth Amendment rights and deprived AT&T of procedural and substantive due process, and that Delaware's escheat law was void for vagueness and preempted by federal common law, among other allegations. In response, the department filed an action in Delaware's Court of Chancery seeking an order compelling AT&T to comply with the subpoena. AT&T responded by filing a motion to stay the state litigation in favor of the federal litigation (which the chancery court denied, [citing the *Univar* decisions for support](#)) or, in the alternative, to quash or modify the department's subpoena. AT&T advanced a number of arguments why the subpoena was not reasonable, including that the subpoena sought information and records dating back to 1992 for years that were barred from assessment due to the

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expiration of the statute of limitations and that the department lacked authority to review checks issued to individuals with addresses outside Delaware.

The chancery court acknowledged that it had not previously articulated the framework to govern an action to enforce an administrative subpoena under the Delaware Escheats Law. The court concluded that Delaware law requires an inquiry into the reasonableness of an administrative subpoena, though this standard would be deferential to the State Escheator. Notably, in articulating this conclusion, the court relied on the Alston & Bird–authored BNA portfolio for the principle that “[h]olders expect both the conduct and the review methodology employed by unclaimed property auditors to be reasonable.”

The court went on to explain that the agency bears the initial burden of showing that the subpoena is authorized, in which case the burden would be shifted to the respondent to prove that enforcement would be improper. Although the court found that none of AT&T’s individual theories established that the subpoena falls outside the State Escheator’s authority—the arguments are more relevant to the state’s authority to bring an enforcement action rather than conduct an investigation—it ultimately held that the theories “collectively” established that the subpoena was “overly broad and unreasonable” and that to enforce it would abuse the court’s process.

In particular, the court found the following:

- The subpoena was too expansive “as to the time period it covers and the subject matter it embraces.” The subpoena sought information going back to 1992, and the department failed to provide any rationale for why it was seeking information going so far back. The court determined that “[t]he Department seems to be pursuing information about property that it knows it cannot recover, and it ... supported those requests with only bareboned allegations.”
- The court also found similar problems with the subpoena’s subject matter, because the department requested “records regardless of whether the last-known address as reflected on AT&T’s records was located in Delaware.” The court noted that “[u]nder *Texas v. New Jersey*, the State Escheator can only seek to escheat property where (i) the last known address is in Delaware or (ii) the company is domiciled in Delaware and (a) there is no last known address or (b) the last known address is in a jurisdiction that does not escheat property.” The court further held that “[b]ecause the State Escheator can never reach property that does not fall into one of the escheatable categories, the State Escheator acts at the outer limit of its auditing authority when it requests records involving that type of property.”
- Further, the court objected to the department’s request for records of all checks, regardless of whether they had been cashed, voided, or were still outstanding, characterizing this as a “massive request for information” without any rational basis for needing it articulated by the department. The court held that the burden for the department’s request for check records is on the department to prove that voided checks constitute unclaimed property. Once again, the court noted that “the Department seems to be pursuing information about property that it knows it cannot recover, and it failed to support those requests with any creditable explanation.”

Ultimately, the court determined that the subpoena would “sweep in a vast amount of irrelevant data” and that the department had no credible explanation of why it needed this data. The court did acknowledge that the department “might have good explanations on these points” but had declined to provide them.

In addressing AT&T’s statute of limitations argument, the court faced the prospect of a statute of limitations amended during the AT&T audit. When the audit began in 2012, Delaware’s statute of limitations for issuing an assessment was three years from the date that the holder files an annual report. In 2017, the state amended the statute of limitations, which provided a 10-year limitations period that could be tolled by the State Escheator’s delivering a notice of examination. The department asserted (without explanation) that the 2017 version of the statute of limitations applied retroactively to AT&T’s audit. The court dismissed the department’s assertion and stated that such an application “would break with the time-honored principle that Delaware courts will not infer an intention to make an act retroactive and that to give an act a retrospective operation would be contrary to well settled principles of law applicable to the construction of statutes.” According to the court, then, both the 10-year statute of limitations and the tolling provision apply only to audits that began in February 2017 or later.

Notably, the court also opined on the “larger picture” of states’ escheat laws that have “come under assault for being exploited to raise revenue rather than to safeguard abandoned property for the benefit of its owners.” The court observed that the department’s subpoena is cause for concern that Delaware is seeking to raise revenue rather than safeguard abandoned property. The court further noted that in delegating the AT&T audit and subsequent investigation to Kelmar, the state divorced itself from “any meaningful involvement in the investigation” and “the Department appear[ed] to have lent the State Escheator’s investigatory authority to Kelmar to use as it sees fit.”

The court also called out Kelmar’s incentives for engaging in aggressive enforcement tactics. The court noted that Kelmar’s relationship with Delaware “potentially creates a pernicious incentive for Kelmar to service broad information requests and engage in expansive audits that impose substantial burdens on companies, thereby inducing settlements that generate income for Kelmar” because Kelmar is compensated based on the amount of property escheated to the state. The court also suggested that Kelmar’s insistence on obtaining records for all checks—regardless of the owner’s last known address—could relate to the fact that Kelmar audits on behalf of other states. Thus, these records “would be helpful to Kelmar in recovering property for other states, but helping other states recover property is not a purpose of the Escheat[s] Law.” However, it is worth noting that (according to documents filed in the case) under Kelmar’s new contract with Delaware effective January 1, 2020, Kelmar is compensated on an hourly basis, except for securities audits, which have a 12% contingency fee.

Despite the court quashing the department’s subpoena, the department decided to file a motion for reargument. Depending on the outcome of the motion for reargument, the department could craft a new, more narrowly focused subpoena. Regardless of the eventual outcome at the state court level, though, many of the broader legal disputes will presumably ultimately play out in federal court.

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