



# This Week in State Tax (TWIST)

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## Delaware: Unclaimed Property Notices Mailed; Companies Have 90 Days to Respond to Invitation Letters

The Delaware Secretary of State's Office (Secretary) has confirmed that on or around July 14, 2023 it mailed letters to companies inviting them to join the state's Unclaimed Property Voluntary Disclosure Agreement (VDA) Program.

As stated in previous mailings, companies that do not respond and enroll in the VDA Program within 90 days of the date of the letter will be referred to Delaware's Department of Finance for audit. As such, it is imperative that companies be on the lookout for these mailings and respond in a timely manner.

### Background

The VDA invitation letters are usually addressed to a company's Chief Financial Officer or other high-level executive and can be easily overlooked. Companies at risk of receiving this outreach have historically ranged from middle-market companies through Fortune 100 companies, both privately and publicly held, across a wide range of industries including oil and gas, retail, banking, utilities, technology, media, healthcare, manufacturing, pharmaceutical, and consumer products. Companies that do not file unclaimed property reports, have not recently been audited by Delaware for unclaimed property, and/or have not recently completed a VDA with the state should be on heightened alert.

Further, we have observed a marked increase in the receipt of audit notices and other state correspondence by companies that either (A) have a long filing history but may have made recent acquisitions that caused them to acquire liabilities, (B) have inadvertently excluded certain categories of property typical of their industries, or (C) companies that have formed within the last ten years but have experienced growth that has outpaced their compliance programs (e.g., start-ups that have recently gone public, software-as-a-service companies, and companies with online and transient customer bases such as payment processors and online marketplaces). While many of these companies may believe they have minimal unclaimed property exposure, providing records for the entire VDA lookback period and completing the program is often challenging.

In both unclaimed property audits and the VDA Program, Delaware state law requires a look-back period of ten report years, plus the five-year dormancy period for most property types, which equates to a 15-year transactional review period. With many companies unable to readily produce complete accounting records for the entire lookback period due to constraints like system limitations and record retention policies, both types of reviews can be challenging. Further, Delaware law authorizes the use of an estimate to account for periods in the review where complete books and records are not available. In many instances, there is a risk that estimation (a liability typically not already accounted for on a company's balance sheet) may be necessary.

## Considerations for Businesses Receiving an Invitation Letter & Benefits of the VDA Program

While both programs share the same lookback period, there are significant benefits to enrolling in the VDA Program versus being selected for audit, which include but are not limited to:

- **Waiver of Delaware’s statutory penalties and interest charges.** All penalties and interest are waived for companies that complete the VDA Program in good faith. By contrast, the State Escheator’s authority to waive penalties and interest for companies under audit is limited. For audits authorized on or after August 1, 2021, a 20 percent assessment of interest on past due property uncovered (including estimated amounts) is now considered “un-waivable,” unless a company elects participation in an “expedited audit” option, which contains its own risks and an “un-waivable” one percent interest assessment.
- **More favorable review criteria.** A 90-day aging criteria for voided disbursement checks applies under the VDA Program, while a normal audit uses a 30-day period and presumes that all checks voided more than 30 days after issuance are unclaimed property liabilities unless the company under audit can prove otherwise. This can provide a substantial benefit in terms of reduction of volume of checks requiring review, as well as the associated dollars of potential exposure.
- **Control over the process.** Under the VDA Program, a company is allowed to perform a “self-review” of its own records to identify and remediate areas of exposure. This contrasts with a standard audit in which third-party auditors will review all records and entities that they determine are “in-scope,” can require extensive supporting documentation to support any claims that assessed items are not unclaimed property liabilities, and can calculate their own assessments of liability that must then be refuted by the company under audit.
- **Limited options.** As previously noted, businesses that do not enroll in the VDA Program may be selected for audit by Delaware’s Department of Finance and State Escheator. For audits authorized after August 1, 2021, businesses may request an “expedited” audit program. Considerations related to the “expedited” audit program include:
  - Expedited audit requests by businesses are granted or denied at the sole discretion of the State Escheator within 60 days of the request. If accepted, a holder must provide “sufficient responses” to auditor requests within prescribed timeframes generally following an 18-month timeline. If a holder provides sufficient responses during the expedited audit, the Escheator must provide an audit report within two years, as compared to historical audits that have typically taken three to five years (or more) to complete.
  - The State Escheator cannot waive the 20 percent assessment of interest on past due property for audits authorized on or after August 1, 2021. However, if a business elects to resolve an examination through the expedited audit process, it may only be subject to a reduced one percent interest assessment.

### KPMG Observations

Holders of unclaimed property that received audit notices from Delaware are often companies that did not respond to an invitation to participate in the Delaware’s VDA Program or were undergoing a multi-state unclaimed property audit. Delaware’s unclaimed property law allows the state to initiate audits of companies without first sending a VDA invitation if (A) an audit was initiated by another state, (B) the company applied for or entered into a VDA with Delaware prior to June 30, 2012, or (C) the company enrolled but later withdrew from Delaware’s VDA program on its own or was removed from the program due to not working in good faith to complete the program.

There are many companies receiving audit notices right now that did not respond to VDA invitation mailings that went out earlier this year. Companies receiving *audit notices* should consider the following:

- Securing a non-disclosure agreement with Delaware or—most often—the third-party audit firm conducting the audit on behalf of multiple states, prior to disclosing any information to the auditor.
- Requesting a list of states invited to participate in the audit—as well as copies of all state audit notices sent—from the third-party audit firm conducting the audit to confirm the auditor is indeed authorized to be conducting the audit on behalf of the state.
- How the company’s fact pattern may limit the scope of the audit (e.g., entities divested via stock acquisition, entities that underwent bankruptcies, etc.) and whether the auditors are entitled to receive all information being requested (e.g., data requests extending beyond the lookback periods employed by the states, etc.).
- The periods for which records are available and/or researchable, which will be important as the auditors will use certain “base years” to develop error ratios for the calculation of potential estimated assessments for the state(s) of incorporation participating in the audit.

Companies that receive a VDA invitation letter, a compliance review notice, or an unclaimed property audit notice from Delaware or other states should evaluate next steps and risk areas related to unclaimed property non-compliance. Additionally, companies that are incorporated in Delaware but are not in compliance and have not yet received an invitation should proactively assess their overall compliance with unclaimed property and consider enrolling in Delaware’s unclaimed property VDA Program.

### **Contacts**

For more information, please contact Will King | +1 (214) 840-6107 | [williamking@kpmg.com](mailto:williamking@kpmg.com), or Marion Acord | +1 (404) 222-3053 | [marionacord@kpmg.com](mailto:marionacord@kpmg.com).



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