

# Abandoned and Unclaimed Property

As Related to Healthcare



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## Agenda



- What is Unclaimed Property?
- Overview of Current Environment
- Audit Experiences
- Voluntary Disclosure Agreements (VDA)
- Healthcare Specifics and Example

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## What is Abandoned and Unclaimed Property (“AUP”)?



- Property that has not been claimed by an “owner” for a specified period of time (dormancy period) is considered abandoned or unclaimed.
- After statutorily defined holding periods, the “holder” of the property has an obligation to file annual reports and remit the unclaimed property to the appropriate state(s).
- In excess of one hundred types of property are considered potential types of unclaimed property by the states.
- States have become increasingly aggressive recognizing this as a good source of non-tax revenues.

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## Common Definitions



- Abandoned (Unclaimed) Property: Tangible or intangible property that has gone unclaimed by its rightful owner.
- Activity: Action taken on property by the owner which may include making a deposit, a withdrawal, a written memorandum to the holder or any action that state statute deems adequate.
- Aggregate: The threshold dollar value of an individual owner’s account which will require owner detail and due diligence efforts. (Example: if the aggregate is \$25 – all individual accounts equal to or greater than \$25 must be identified on the report and due diligence performed).
- Custodian: An individual or entity which holds property until it is delivered to the rightful owner. Most states’ laws make the unclaimed property division a “custodian” of the property remitted to the state.
- Due Diligence: The degree of effort required by law that a holder must perform to find the rightful owner before remitting the property to the state.
- Dormancy Period: The period of time that transpires since the last date in which an owner generated any action on his or her property.

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## Common Definitions



- Dormancy Date/Date of Last Activity: The date of last contact by the owner as evidenced in the records of the holder.
- Escheat: A transfer of property that makes the state the legal owner of the transferred property. Few states operate under an “escheat” law as it relates to unclaimed property.
- Holder: The entity that is in possession, or controls the property until it is transferred to the Custodian on behalf of the lost owner.
- Indemnification: An agreement that protects a party from loss by transferring the responsibilities to a third party.
- Intangible Personal Property: Property that is represented by a symbol. Stock certificates and savings bonds represent ownership interest in a company. A savings bond represents an obligation to pay the face value.
- Rightful Owner: A person/entity which has the legal right to the property.

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## Sourcing Rules



- 1st Priority Rule: State of owner’s last known address
- 2nd Priority Rule: Holder’s State of Incorporation, if the last known address of the owner is unknown
- Throwback Rule: In the event the jurisdiction of the owner’s last known address does not escheat property, then the State of Incorporation may claim property
- Third Priority Rule: Some states claim that if there is no last known address and if the State of Incorporation does not escheat the property type, it may be sourced to state where the transaction took place

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## Sourcing Rules - Extrapolation



- Lookback periods vary by state and are generally determined by auditor practice as opposed to legislation
- Lookback periods are generally 10 to 15 years
- Due to the lack of data in prior periods, an extrapolation methodology may be used to determine an estimate of property due for that period.
- All estimated or extrapolated property is unknown, and therefore, consistent with priority rule #2, due to the Holder's State of Incorporation

Example: Company has addressable outstanding checks of \$20,000 each year for the years 2000-2006 totaling \$140,000 after research. Company revenues are \$500 million each year for the years 2000-2006 and decreased by \$10 million each prior year going back to 1981. The extrapolation for the years 1981-1999 would total \$304,000 making the liability for outstanding checks \$444,000 for the years 1981-2006.

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## Overview of Current Environment



- Third-Party audits have increased. The major audit firms are Kelmar, ASUS, ACS and SAS.
- ACS has currently sent audit notices out to healthcare providers as well as educational institutions, focusing on outstanding checks as well as Accounts Receivable credit balances.
- Kelmar is currently conducting the majority of Delaware audits and has increased its representative states outside of Delaware.
- All property types are being reviewed (Accounts Payable, Payroll, Accounts Receivable, Benefits, Inventory, Rebates and Equity, etc.).
- "Linkage Letters" are being requested from Holder representatives to attest how far back records are available.
- Statistical Sampling is widely used to determine liability.

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## Current Trends



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## Audit Experiences



What occurs during an unclaimed property audit?

- Significant resource drain (accounting, tax, IT, finance, legal) regarding audit defense and the gathering of accounting records. Audits will usually cover periods back to 1981, giving consideration to prior audits.
- Third party auditor will often be paid on a contingent basis and will be aggressive pursuing large settlement offers. Third party auditor may seek to expand the audit to multiple states.
- Review of areas not often examined, even in a tax audit (e.g., credits in the Accounts Receivable and Inventory areas, outstanding checks from self insured medical plans, unexchanged shares, etc.).
- The auditor’s presumption is that the property is unclaimed unless the records and/or procedures establish otherwise. Often times, records do not rebut the presumption that an item is escheatable.
- Lengthy process of interpreting data and negotiating unclaimed property treatment of certain issues.
- Auditors are likely to request massive volumes of information.
- If audit does not progress in a timely manner, material interest and penalties will be assessed.

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## Voluntary Disclosure Agreements (“VDA”)



- Audits are becoming more common as many states have increased efforts to enforce their unclaimed property laws.
- Initiating the filing of unclaimed property reports on a prospective basis could trigger an audit.
- If the unclaimed property exposure is significant, a VDA might be the best solution.
- A VDA involves negotiating with the state(s) to bring holders unclaimed property filings current and close out prior year liabilities.
- Under most VDA’s the state(s) may waive penalties and limit the number of prior years for which the liabilities are due.

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## Benefits of VDAs



- Limited lookback period
- Self Review process
- Waiver of penalties
- Waiver of interest (most states)
- Indemnification from owners and states
- Ability to re-evaluate/ release reserves

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# Areas of Review for Healthcare Providers



## Potential Unclaimed Property Issues Affecting Hospitals:

- Large amounts of deposits and/or credits on accounts
- Maintenance of detailed records for some period of time related to credit balances, but due to the change in customer base (patients) often, the details will not be maintained over a long period of time
- Multiple payees on most invoices (insurer(s) and patient)
- States are interested in the amounts that are currently outstanding, as well as the calculated amounts potentially written off or amounts where detailed address information has been purged
- High potential for accounting errors associated with continually changing rate cards from multiple insurance companies

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# Areas of Review for Healthcare Providers



## Areas of Review:

- Outstanding vendor and payroll checks;
- Customer overpayments and/or unutilized credits;
- Accounts that are closed with credit balances remaining; and
- Unapplied cash due to the lack of invoice information

## Current Issues Related to Third Party Audits:

- Netting of Debits vs. Credits for customers when reviewing AR;
- Current Customer Exception or Business-to-Business Arguments; and
- Testing methodology.

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## Healthcare Provider Examples



### Hospital #1 - Approximately 1,200 beds

Total initial estimate was around 9 million dollars, of which 70% was related to patient credits.

Areas of Exposure:

- Accounts Payable/Vendor Checks
- Payroll Checks
- Patient Credits
- Insurance Overpayments

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## Healthcare Provider Examples



### Hospital #2 - Approximately 400 beds

Total initial assessment was around 3 million dollars, most of which was related to patient credits and insurance overpayments.

Areas of Exposure:

- Accounts Payable/Vendor Checks
- Payroll Checks
- Patient Credits
- Health Benefits
- Patient Refund Checks
- Unidentified Remittances

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