26th Annual Health Sciences Tax Conference

Unclaimed property: fundamentals, reporting responsibility and the changing environment

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Presenters

► Donna Wallace, CPA
SSM Health
St. Louis, MO

► Jennifer Richter
Ernst & Young LLP
St. Louis, MO
jennifer.richter@ey.com
+1 314 290 1024

► Aurianne Lopatka
Ernst & Young LLP
Boston, MA
aurianne.lopatka@ey.com
+1 617 585 0934
Agenda

► Unclaimed property fundamentals
► Property types specific to health care providers and insurers
► Health care and health insurance audit campaign
► Recent litigation and implications
► Challenges to maintaining compliance
► Best practices for effective annual compliance
Unclaimed property fundamentals
Unclaimed property (UP) at a glance

- UP represents a liability due and owing to another party.
- Tangible or intangible property unclaimed by its rightful owner after a period of time is called the dormancy period.
- UP is not a tax, but a property right.
  - It is often referred to as a “hidden liability” and is remitted dollar for dollar (generally).
  - No nexus or tax rate considerations.
- An organization’s UP footprint can be heavily impacted by underlying accounting policies.
  - Property may be currently on the general ledger in the form of uncashed checks or not visible due to void or write-off policies.
Priority rules


Priority rules summary:

- **First priority** — State of last known address
- **Second priority** — State of incorporation or formation if last address is unknown or if the address is a foreign address (generally)
- **Business impact of priority rules** — Annual compliance reporting on a multistate basis (usually 50) while estimated historical payments and settlements are paid to state(s) of incorporation or formation
Compliance requirements

► Not uncommon to have a 50-state reporting obligation
► All 50 US states (plus District of Columbia, Puerto Rico, Virgin Islands and Guam) maintain unclaimed property statutes
► Companies are required to file UP annually with the applicable state
► Dormancy periods and exemptions differ by state
► Some states require negative or zero reporting
► Statutory due diligence letter mailings to owners with specific timing prior to escheatment
Specific to exempt organizations

► To our knowledge, Colorado, Kentucky and Ohio have 501(c)(3) reporting exemptions.
► There are still requirements to file outside of these three states:
  ► Insurance reimbursements, overpayments and refunds due to out-of-state insurance companies
  ► Vendor payments to out-of-state suppliers
  ► Vendor payments to other out-of-state goods and services providers
Property types specific to health care providers and insurers
Common property types for organizations (varies by industry)

- Uncashed checks: payroll, vendor, refund, interest, dividends, royalties
- Accounts receivable credit balances
- Unredeemed gift cards
- Merchandise credits
- Customer overpayments
- Unapplied cash or unidentified remittances
- Unused deposits
- Dormant bank accounts
- Insurance proceeds
- Health expense accounts
- Consumer or customer rebates
- Securities-related property
- Stocks, mutual funds
- Benefit-related property
- Traveler’s checks and money orders
Property types specific to health care providers and health insurers

Provider side:
- Patient billings, overpayments and refunds due
- Insurance reimbursements, overpayments and refunds due
- Provider reimbursement

Insurance side:
- Claims payments
- Premium refunds due
- Member and provider overpayments
- Medicaid reimbursement and payment integrity
- Health Insurance Exchange (HIX) marketplace reimbursement and payment integrity
Health care and health insurance audit campaign
Typical general ledger audits

- Contract audit firms: Kelmar, Xerox, PRA Government Services, Specialty Audit Services
- Focus on transactions booked to the general ledger
  - Accounts payable (AP), payroll, accounts receivable (AR) credits, benefits, gift cards, rebates, refunds, stocks, bonds, dividends, etc.
- Address property due to states of last known address
- Owner-unknown property due to state(s) of incorporation or formation
- Estimation by its very nature is owner-unknown property
- Reachback under audit can be 15 years (generally 10 years plus dormancy period)
  - Delaware is unique in its approach
Targeted audits
Verus Financial

► Exam notices indicate:
  ► “Property related to the administration of health insurance and the provision of health-related products and services” will be reviewed.
  ► The focus is on rebates, refunds, reimbursements, individual enrollees, employee groups and providers.

► Focus on process or method to record the transaction
► Reachback under audit can be 15 years (generally 10 years plus dormancy period)
  ► Delaware contracts with Verus, but to date, Delaware is not involved in the health care audit campaign.
  ► To the extent that a company has records for a full audit period, the property reviewed is limited to property whose owner has an address in an audit-participating state.
Probable audit focus

► Medicaid and HIX marketplace program problem areas:
  ► Tracking of enrolled, re-enrolled and terminated members
  ► Medicaid churn and retrospective enrollment and termination
  ► Deceased members
  ► Billing, claims and roster discrepancies
    ► Collection of overpayments with providers and vendors
    ► Unpaid claims and physician reimbursement
  ► Verification of services and program integrity
  ► HIX only — Member premium refunds and payment issues
Probable audit focus

► Seeming similarities to a recovery audit contractor audit
► Further difficulties
  ► Extracting data from systems, currently and historically
  ► Difficulties in reviewing and analyzing the data — goes beyond traditional financial, accounts receivable and property
Recent litigation and implications
Legislative environment

► On June 28, 2016, the US District Court for the District of Delaware issued its opinion in *Temple-Inland, Inc. v. Thomas Cook* maintaining that Delaware’s executive action of auditing and assessing a multistate corporation’s unclaimed property violated substantive due process.

► Delaware’s actions, when taken together, “shock the conscience.”
  ► No record retention statute specific to UP
  ► Yet audits go back 20+ years
  ► Estimation calculations can create significantly misleading results
  ► Delaware in the best position to remedy its deficiencies

► Significant impact on unclaimed property audits involving estimation not only by Delaware but other states as well
Legislative environment

- Unexpected settlement on August 5, 2016 — Delaware and Temple-Inland filed a joint motion to dismiss the case with prejudice.
- The voluntary and confidential settlement agreement “fully and finally resolves all claims.”
- The case will not be appealed to the US Third Circuit Court of Appeals by either party, as originally anticipated.
- The Court’s June ruling stands.
- The settlement does not provide for the “remedy” that the judge initially requested of Delaware.
- Delaware is currently reviewing its audit procedures and unclaimed property statutes and we anticipate: 1) a slowdown in the amount of settlements or extrapolation payments received until clearer guidance is communicated and 2) potential changes to the “existing” extrapolation method utilized, as well as further limitations on look-back.
Challenges to maintaining compliance
Observed challenges

- Keeping up with legislative changes or significant cases — How do they impact strategy and industry insight?
- Resource drain — The knowledge required for completing an unclaimed property review often requires significant input from many areas of the company.

<table>
<thead>
<tr>
<th>Department</th>
<th>Example needs</th>
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<tbody>
<tr>
<td>Legal</td>
<td>Support interpretation and analysis of statute</td>
</tr>
<tr>
<td>Tax</td>
<td>Organizational structure, history and tax return information</td>
</tr>
<tr>
<td>Accounting/general ledger</td>
<td>Queries or reports from operating system, tie-out support and detailed transactional research</td>
</tr>
<tr>
<td>AP, AR, Finance</td>
<td>Policies and procedures, customer and vendor relationships and remediation research</td>
</tr>
<tr>
<td>IT</td>
<td>Assistance with system changes or special reporting, understanding capabilities and archived systems</td>
</tr>
<tr>
<td>Marketing</td>
<td>Customer policies, gift card or promotional programs</td>
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<tr>
<td>Treasury</td>
<td>Bank account landscape and history</td>
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<tr>
<td>Human Resources</td>
<td>Understanding benefit plans, third-party administrators and history</td>
</tr>
</tbody>
</table>
Observed challenges

► Data management — Gaining access to archived records and managing extremely voluminous data
► Presumption of abandonment — Burden of proof on holder and remediation
► Gaps in existing process — Not evaluating all relevant property types, legal entities or business units
► Establishing and adhering to sound UP policies and procedures across the organization (such as write-off policies within billing systems or bank reconciliation processes)
► Streamlining an effective data gathering process from various business units, enterprise resource planning (ERP) systems and functional areas within the organization
► Limited in-house resources for administering the unclaimed property compliance function, with risk of institutional knowledge loss upon attrition
Observed challenges

► Some companies underutilize reporting software due to a lack of training or knowledge beyond basic functionality.
► UP can be overreported by not considering available exemptions and deductions, such as business-to-business, payroll, de minimis, cost of goods sold for gift cards and merchandise credits and other items.
► A proper audit trail should be established and maintained through policies and document retention so as to enable the organization to rebut the presumption of abandonment for specific transactions.
► Challenges associated with mergers and acquisitions can include inheritance of predecessor UP liability, or difficulty integrating new operations into centralized and consistent filing processes.
► System upgrades and conversions should always be evaluated with a UP point of view to avoid loss of data, mass write-offs and “cleanups” and potential red flags upon audit.
Best practices for effective annual compliance
Should your business consider a UP review?

► If your business is currently involved in, or planning, any of the following events, you should consider a UP review:
  ► Ongoing or new UP audits underway
  ► Filing of voluntary disclosure agreements with respect to state(s) of incorporation and formation
  ► No prior filings in state(s) of incorporation and formation
  ► Merger and acquisition activity
  ► Filing annual UP reports and no recent review of internal process

► You should also consider a UP review if the following apply:
  ► Lack of visibility into historical liabilities
  ► Decentralized ERP systems, billing systems or banking landscape
Action plan

► Obtain and review core accounting policies and procedures, sample agreements and other business model documentation to enable risk assessment

► Gauge potential exposures based upon:
  ► Prior filing history
  ► Accounting flow of aged, uncashed checks and accounts receivable credit balances to an unclaimed property general ledger account
  ► Due diligence policies and practices
  ► Contracting practices and business models
  ► Impact of outsourcing arrangements of unclaimed property reporting function (such as with third-party benefit providers)
  ► Knowledge of state dormancy standards and exemptions
Improvements for state Medicaid and HIX marketplace programs

► Standardize file formats used by analysts
  ► Example: Member Roster files differ in every state (incoming method, columns and information, required fields)
  ► Reduce errors by reformatting and standardizing the files before sending to membership and enrollment

► Make compliance, verification and reconciliation a priority
  ► Many payors do claim audits and compliance activities, but some key areas have historically been a lower priority due to the lack of enforcement or penalties
  ► Example: Duplicative members enrolled; premiums for retroactively terminated or deceased members; billing for termed or deceased members

► Standardize, and possibly automate, enrollment and disenrollment processes
  ► Many payors require enrollment analysts to verify the following: death rosters, state active member websites, past and duplicative member records
  ► Use multiple personal or demographic inputs to look for duplicates or find members
  ► Increase automation to reduce human error and process variance

► Audit claims and billing IT systems to ensure accuracy for multiplan members
  ► Medicaid is the payor of last resort; systems are often not coded when members have multiple health plans such as Medicare, Medicaid, Long-Term Services and Support, Development Disabilities, Behavioral Health, Indian Health, commercial plans
Appendix
Glossary of terms
Common terms

*These are presented for discussion purposes only, as relevant to this presentation, and do not represent legal definitions in any way.*

- **Holder** — Entity that issues or controls the property until it is transferred to the appropriate state upon escheatment; organization (legal-entity specific)
- **Owner** — Entity having a legal or equitable claim to the abandoned property; employees, vendors, customers, etc.
- **Custodian** — Holds and controls property until delivered to the rightful owner; the state
- **Dormancy period** — The period of inactivity (usually one, three or five years) after which property is considered abandoned
- **Escheat** — Transfer of property to the state where the owner was last known to reside
Common terms

► **Escheatable** — Describes property identified as abandoned and to be reported

► **Extrapolation** — An estimate of the property that should have been reported for a time period in which there are no detailed records to support the liability

► **Actuals** — Refers to detailed records that identify and support UP liability

► **Owner unknown property** — Property identified as potentially escheatable and for which no owner-addressable information can be identified on books and records; may include extrapolation values

► **Addressable property** — Property identified as potentially escheatable and for which a complete name and address is available per books and records
Questions?
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