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# State Tax Return

## A Due Process Clause Challenge To The Uniform Unclaimed Property Act's Transactional Test For Taking Unclaimed Property

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### A Brief History Of Unclaimed Property Law

Governments have long claimed the right to take possession of abandoned or unclaimed property, a right known at common law as "escheat." Escheat law began as a way for the government to claim real property left by a decedent who had no heirs. Rather than leaving the property to languish in the decedent's estate, the sovereign would take title and return the property to a useful purpose. This power was a natural incidence of sovereignty. As William Blackstone reminds us, "all lands were originally granted out by the sovereign, and are therefore holden, either mediately or immediately, of the crown." William Blackstone, 2 Commentaries on the Laws of England 53 (William Draper Lewis ed., Rees, Welsh & Co. 1898). The concept later grew to include a sovereign right to claim personal property left by decedents without heirs, known as *bona vacantia*. These concepts, like so many other English common law doctrines, traveled to the American colonies.

The field of unclaimed or abandoned property law in our country grew during the 20th century to encompass both of the older doctrines of escheat and *bona vacantia*. States enacted statutes that lay claim to all forms of property that met a statutory definition of "abandoned property," which usually included a relatively brief period of dormancy. The statutes, moreover, covered *all* unclaimed property, not merely that left behind by a decedent with no heirs.

States became increasingly interested in unclaimed intangible property and soon discovered that a host of businesses held unclaimed balances for all sorts of accounts and services. Pennsylvania, for example, discovered that Western Union maintained millions of dollars in unclaimed money orders on their books. See *Western Union Tel. Co. v. Pennsylvania*, 368 U.S. 71 (1961). And other states recognized the value of unclaimed stock and dividends held by corporations and securities intermediaries. See

*Delaware v. New York*, 507 U.S. 490 (1993). These sources of cash prompted states to enact abandoned property laws specifically covering intangible personal property. The U.S. Supreme Court has generally upheld the constitutionality of a variety of state abandoned property laws. Those laws, the Court has said, ensure that abandoned property ends up in the state's hands where it can be put to use benefiting the public, "rather than for the chance enrichment" of the individual or organization that happens to be in possession of the property at the time it became abandoned. *Standard Oil Co. v. New Jersey*, 341 U.S. 428, 436 (1951).

### **Conflicting State Escheat Claims, *Texas v. New Jersey*, And The Uniform Unclaimed Property Act's "Transaction" Test**

The growing state interest in unclaimed intangible personal property led the National Conference of Commissioners on Uniform State Laws ("NCCUSL") — the same group that brought us the Uniform Commercial Code, among other laws—to draft and approve a Uniform Unclaimed Property Act in 1954. The Act responded to the concern that a holder of unclaimed property could be subject to conflicting escheat claims from two different states. The concern arose from two U.S. Supreme Court cases: *Connecticut Mutual Life Insurance Co. v. Moore*, 333 U.S. 541 (1947), which held that the state in which the unclaimed property's true owner had his last known address could claim the property; and *Standard Oil Co. v. New Jersey*, *supra*, which held that the state of the unclaimed property holder's incorporation could claim the property. These two cases encouraged a "race of diligence" to see which state could reduce its claim to judgment first and obtain the unclaimed property. Section 10 of the 1954 Uniform Act dealt with this problem by generally giving the priority claim to the state of the last known address of the abandoned property's owner, thus providing some means of avoiding a "race of diligence" in determining which state could claim the abandoned property while avoiding the imposition of double liability on the abandoned property holder.

The U.S. Supreme Court, too, weighed in on the subject of conflicting state escheat claims in *Texas v. New Jersey*, 379 U.S. 674 (1965), and, like the Uniform Act, resolved the conflict in favor of the state of the true owner's last known address. Texas and New Jersey both tried to claim abandoned property held by the Sun Oil Company. New Jersey relied on its power to claim the property as the state in which Sun Oil was incorporated, a power recognized by the U.S. Supreme Court in *Standard Oil*. Texas claimed the right to the property as the state of the last known address of the true property owners, a power recognized in *Connecticut Mutual Life Insurance Co.*

The Court, relying on its original jurisdiction to resolve disputes between the states, created a priority scheme, giving the first right to claim abandoned property to the state of the true owner's last known address. That state would have been Texas. If the holder's records did not reflect a last known address, or if the state of last known address had no applicable unclaimed property law, then the state of incorporation for the property holder could claim the property. That state would have been New Jersey. New Jersey's claim, moreover, would be subject to a later claim by the last-known-address state if the last known address were later discovered or if the last-known-

address state enacted a law covering the unclaimed property in question. The U.S. Supreme Court has stood by its scheme, unmodified, in two subsequent cases: *Pennsylvania v. New York*, 407 U.S. 206 (1972), and *Delaware v. New York*, 507 U.S. 490 (1993).

The NCCUSL eventually incorporated *Texas v. New Jersey* into the Uniform Unclaimed Property Act beginning in 1981. Section 3 of the 1981 Act gives the priority escheat claim to the state of the true owner's last known address with the second claim going to the state of the holder's incorporation. Section 4 of the 1995 Act incorporates the *Texas v. New Jersey* scheme in a similar fashion. Today, 41 state have enacted some form of the Uniform Acts, with most using either the 1981 or the 1995 version.

Although *Texas v. New Jersey* answered many questions, it did not answer them all. What happens if an abandoned property holder does not know the last known address of the true owner and the law of the holder's state of incorporation does not provide for the escheat of the abandoned property? *Texas v. New Jersey*, and the Uniform Act provisions incorporating the decision, are of little help. Without a last known address for the true owner, the first priority state remains a mystery and obviously cannot claim the property. But the second-in-line state of incorporation also cannot claim the property because its law does not cover unused balances on gift cards. Which state can claim? The Supreme Court has not answered the question.

The NCCUSL, however, has answered the question and said that in this situation, the state where "the transaction out of which the property arose" can claim the property. See 1981 Uniform Unclaimed Property Act, § 3(6); 1995 Uniform Unclaimed Property Act, § 4(6). Although the NCCUSL Commissioners described this rule as allowing a state with "a genuine and important contact with the property" to stake a claim, the actual text itself is remarkably vague. See 1981 Uniform Unclaimed Property Act § 3 Comment. The text itself does not define the term "transaction" and neither have the courts. The dearth of case law interpreting the transactional test no doubt stems from the uncertainty over the test's reach. As one group of commentators put it, "[i]t is quite possible that the practical difficulty of pursuing transactional claims has deterred collection efforts by the various states that have enacted transactional tests." Michael Houghton, et al., *Unclaimed Property*, 74-2nd C.P.S. (BNA 2004), at A-35. But, as explained below, the uncertainty surrounding the meaning of the transactional test extends far beyond the frustration of those trying to understand its scope. Rather, the transactional test raises serious constitutional problems as to its enforceability.

## **The Constitutional Problems With The "Transaction" Test**

### ***State Court Jurisdiction And The Due Process Clause***

The uncertainty of the reach and meaning of the "transactional" test raises serious constitutional concerns in light of the U.S. Supreme Court's personal jurisdiction cases. The Due Process Clause from the Constitution's Fourteenth Amendment says that "No State shall . . . deprive any person of life, liberty, or property without due process of

law.” Individuals, moreover, have a recognized liberty interest in being free from the binding judgments of foreign state courts who, for example, may seek to adjudicate an abandoned property claim against them. So when a state court orders an out-of-state holder of unclaimed property to turn that property over to the state escheator, that court has deprived the holder of a liberty interest, which can only be accomplished in accord with the Due Process Clause’s requirements. This effectively limits the reach of a state’s courts and correspondingly the state’s ability to enforce its laws against defendants who do not reside in the state.

But what exactly does “due process of law” mean in terms of subjecting out-of-state defendants to a state court’s judgments? The Supreme Court’s modern jurisprudence began with a tax case, where the State of Washington tried to collect unemployment compensation taxes from the International Shoe Company. *International Shoe Co. v. Washington*, 326 U.S. 310 (1945). The Company had no office in Washington and made no contracts for sales of shoes there, but nonetheless employed salesmen, who did live in Washington, to display shoes and solicit orders. The company argued that it was not subject to suit in Washington because the company had no presence in the state, and thus the Due Process Clause forbade subjecting the company to jurisdiction in Washington.

In defining the limits that the Due Process Clause places on state-court jurisdiction, the Supreme Court held that exercising judicial power over an out-of-state defendant would violate the Due Process Clause unless the defendant had “certain minimum contacts with [the forum state] such that the maintenance of the suit does not offend ‘traditional notions of fair play and substantial justice.’” *International Shoe Co.*, 326 U.S. at 316. The Court acknowledged that the inquiry “cannot be simply mechanical or quantitative,” but rather depends “upon the quality and nature of the activity in relation to the fair and orderly administration of the laws which it was the purpose of the due process clause to insure.” *Id.* at 319. The Due Process Clause “does not contemplate that a state may make binding a judgment . . . against an individual or corporate defendant with which the state has no contacts, ties, or relations.” *Id.*

The first part of the *International Shoe* analysis—whether the defendant purposefully established “minimum contacts” in the forum state—is the “constitutional touchstone” of the due process analysis. *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 474 (1985). This fair-warning principle “gives a degree of predictability to the legal system that allows potential defendants to structure their primary conduct with some minimum assurance as to where that conduct will and will not render them liable to suit.” *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 297 (1980).

To be sure, the due process “minimum contacts” requirement is not particularly onerous. In *International Shoe* itself, the Court held that International Shoe’s employment of in-state salesman was a sufficient contact with Washington such that the state’s judicial power could reach International Shoe, at least with respect to the unemployment compensation taxes that arose specifically from the salesmen’s activity in the state. And in *Burger King*, for another example, the Supreme Court upheld jurisdiction in Florida

when the defendant, despite having no physical presence or property in Florida, nonetheless contracted with a Florida resident and engaged in an extensive course of negotiations with the resident concerning a dispute over the contract.

But despite the apparent ease of satisfying the Due Process Clause, the clause still has its limits. The *Burger King* Court, in addressing confusion among lower courts over the power of a contract with an in-state resident to establish the requisite due process “minimum contacts,” said: “If the question is whether an individual’s contract with an out-of-state party *alone* can automatically establish sufficient minimum contacts in the other party’s home forum, we believe the answer clearly is that it cannot.” 471 U.S. at 478 (emphasis in original). Rather, the “prior negotiations and contemplated future consequences, along with the terms of the contract and the parties’ actual course of dealing[,] . . . must be evaluated in determining whether the defendant purposefully established minimum contacts within the forum.” *Id.* at 479. Thus, the mere creation of a legal relationship in a state cannot amount to a sufficient contact for due process purposes. See, e.g., *Savin v. Ranier*, 898 F.2d 304, 307 (2d. Cir. 1990); *Gray & Co. v. Firstenberg Machinery Co., Inc.*, 913 F.2d 758, 760–61 (9th Cir. 1990).

And even if a defendant might have the requisite “minimum contacts” with a forum state, the Court still requires that the exercise of jurisdiction must comport with “traditional notions of fair play and substantial justice.” *Asahi Metal Indus. Co. v. Super. Ct.*, 480 U.S. 102, 113 (1987) (quotation marks omitted). In *Asahi Metal Industry Co.*, the California courts sought to exercise jurisdiction over a Japanese company who made valve stems for motorcycle tires that eventually found their way to California. The Justices could not agree on whether the mere manufacture and distribution of valve stems into the stream of commerce amounted to the “minimum contacts” required by the Due Process Clause. The Court, however, did agree that regardless of how one decides the “minimum contacts” analysis, the Due Process Clause prohibited California from exercising jurisdiction because it would not comport with the second part of *International Shoe*’s analysis, that is, it would not comport with “traditional notions of fair play and substantial justice.” The Court considered four factors in reaching the conclusion that jurisdiction in California would be fundamentally unfair: (1) the burden on the defendant of litigating in a foreign jurisdiction; (2) California’s interest in resolving the dispute; (3) the plaintiff’s interest in obtaining relief; and (4) the interstate judicial system’s interest in efficient dispute resolution. *Id.* at 113. Considering all of these factors, the Court concluded that exercising jurisdiction over a Japanese company concerning a dispute in which California had no interest in resolving counseled in favor of finding that jurisdiction in California would violate the Due Process Clause.

### ***The “Transactional” Test Under The Supreme Court’s Due Process Clause Jurisprudence.***

The “transactional” test seems to transgress the due process limits outlined by the Supreme Court in *International Shoe*, *Burger King*, and *Asahi Metal Industry Co.* First, the Court has made clear that the mere existence of a contract cannot alone establish the requisite due process “minimum contacts,” but it would seem that the mere fact of a

contract is all that the “transactional” test requires. As previously mentioned, the Uniform Acts do not define the term “transaction,” and the common meaning of the term can be quite broad: Webster’s Collegiate Dictionary defines the term to include “a communicative action or activity involving two parties or things that reciprocally affect or influence each other.” Webster’s Collegiate Dictionary at 1252 (10th ed. 1993). Thus the common meaning of “transaction” would seem to broadly include what the Due Process Clause does not allow: the exercise of jurisdiction, and the escheat of unclaimed property, merely based on the existence of a contract or some other minimal “communicative action or activity” between the holder and true owner which occurred in the state seeking to claim the property.

Second, even if a contract might result in a “transaction” sufficient to satisfy the Due Process Clause’s “minimum contacts” requirement, the exercise of jurisdiction must still comport with “traditional notions of fair play and substantial justice.” Those traditional notions, as explained by the Supreme Court in *Asahi Metal Industry Co.* include: (1) the burden on the defendant of litigating in a foreign jurisdiction; (2) the forum state’s interest in resolving the dispute; (3) the plaintiff’s interest in obtaining relief; and (4) the interstate judicial system’s interest in efficient dispute resolution. 480 U.S. at 113.

Initially, the burdens placed on an unclaimed property holder are already high. According to the Supreme Court’s cases, the potential holder of unclaimed property may already be subjected to suit for the unclaimed property by the state of the true owner’s last known address or the state of incorporation, provided those states have laws covering the unclaimed property. Now the Uniform Acts have added a third jurisdiction to the mix: the state of the “transaction out of which the property arose,” which could be more than one jurisdiction, depending upon how a state chooses to interpret the term “transaction.” Forcing a defendant to prepare for litigation in so many jurisdictions, especially when the holder cannot know whether property will become abandoned at the time of the “transaction,” creates an unfair burden on holders.

Conversely, the state’s interests are exceedingly minimal. States claim abandoned property in order to protect the interests of its citizens as true owners and to ensure that the abandoned property is put to good use instead of enriching the holder. But under the “transactional” test, the State does not even know if the true owner is a state resident, meaning the state’s interest in protecting its citizens’ property is greatly diminished. See *Asahi Metal Industry Co.*, 480 U.S. at 114 (when a plaintiff “is not a [state] resident, [then the state’s] legitimate interests in the dispute have considerably diminished”). Unable to claim that its interest in the unclaimed property serves to protect the state’s residents or the property’s true owner, the only interest a state can claim is its interest in enriching itself with property that will probably never be claimed. But that “interest” does not make a compelling argument that the exercise of the jurisdiction by the transaction state meets “traditional notions of fair play and substantial justice.”

Lastly, the interests of the several states “in the efficient judicial resolution of the dispute and the advancement of substantive policies,” *Asahi Metal Industry Co.*, 480 U.S. at 115, weigh against exercising jurisdiction under the “transactional” test. With the term

“transaction” left undefined, the states are free to devise vastly different meanings for the word and thus vastly different results under the test. This only heightens the burden on defendants who could face a series of different standards in different jurisdictions. Worse still, it could create myriad conflicting claims among states who each believe the “transaction” occurred in their state, thus spawning litigation between the states instead of fostering “the efficient judicial resolution” of the dispute. It takes little imagination to envision these problems, as even the Supreme Court recognized the considerable difficulties in deciding escheat claims based on a “transactional” or “contacts” analysis. Justice Black, writing in *Texas v. New Jersey*, flatly rejected a “contacts” analysis in deciding the Court’s priority scheme because “the test as applied in this field is not really any workable test at all—it is simply a phrase suggesting that this Court should examine the circumstances surrounding each particular item of escheatable property on its own peculiar facts and then try to make a difficult, often quite subjective, decision as to which State’s claim to those pennies and dollars seems stronger than another’s.” 379 U.S. at 679. The transactional test, therefore, works at cross-purposes with the efficient resolution of escheat claims and counsels against concluding that the transactional test meets the strictures of the Due Process Clause.

In sum, the “transactional” test from the Uniform Unclaimed Property Acts leaves much to be desired when compared with the Due Process Clause’s requirements for exercising jurisdiction over out-of-state defendants. True, in many cases, the “transactional” test will pose no due process problem. For example, if a “transaction” occurs in the state where the holder has its world headquarters, then that state will have no problem exercising its judicial power over the holder. But in many other cases, the over-inclusiveness of the term “transaction” leaves many unanswered—and quite troubling—due process questions. ■



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