Caveat Emptor:
When a Merger or Acquisition Yields More Than You Bargained For

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Congratulations! You just successfully completed an acquisition, and the business press and your industry peers have all taken notice. Another group is following your transaction as well: state unclaimed property auditors.

Unclaimed property review, as part of transactional due diligence in a merger or acquisition, often goes overlooked. Armed with this knowledge, state unclaimed property auditors include a company's history of transactions in audit proceedings, and states review M&A activity in their jurisdiction for likely audit candidates. This can lead to a costly process for companies that haven't performed the proper due diligence, as the audit scope can expand to include the acquirer's unclaimed property reporting history, the acquired company's reporting history, plus the reporting history from other, previous acquisitions.

Unclaimed property due diligence can have a direct impact on a deal price. If the company is not in compliance with state unclaimed property laws, and has written these unresolved transactions off as income, the acquiring company can be paying an inflated purchase price for the acquisition as well as acquiring the liability, depending on the nature of the acquisition. In an asset purchase, the buyer generally acquires the liabilities that are explicit in the purchase agreement. Under this circumstance, the probability of acquiring an unknown unclaimed property liability is diminished. However, in a stock purchase agreement, the buyer generally acquires all disclosed and undisclosed liabilities.

Investing the time and effort into an unclaimed property review as part of transactional due diligence will enable a buyer to evaluate risk, provide opportunity for mitigation, and reinforce or reevaluate the purchase price of the transaction. The review should include:

- Policies and procedures for resolution of credit balances, unapplied cash, accounts payable and all uncashed checks;
- Policies and procedures for unclaimed property liabilities and reporting;
- Annual unclaimed property reporting history, including copies of reports, voluntary compliance agreements and audit history;
- Exemption and due diligence history;
- Current liabilities that have not yet tolled the dormancy period;
- Third party agreements, including stock transfer agents, payroll administrators, rebate administrators, etc.; and,
- Merger and acquisition history including state of incorporation for all entities.

One factor that can hinder an unclaimed property review is record retention. The preferred record retention period for unclaimed property is at least ten years, since most unclaimed property audit lookback periods are ten years or greater. If the target company was compliant with unclaimed property laws but failed to retain evidence, it could further prolong the review period.

Non-compliance altogether could also delay the acquisition until estimations are completed and mitigation efforts or a resolution plan is implemented.

So, Caveat Emptor. Be sure to include an unclaimed property review in your transactional due diligence. Otherwise, you could end up with an unclaimed property headache and a real case of buyer’s remorse.