



Legislative Fiscal Bureau

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Joint Committee on Finance

Paper #741

Unclaimed Property Program Appropriation Type Conversion (State Treasurer)

Bill Agency

[LFB 2007-09 Budget Summary: Page 520, #3]

CURRENT LAW

The Office of the State Treasurer (OST) is responsible for administering the state's unclaimed property program under Chapter 177 of the Wisconsin state statutes. Under state law, property is generally considered to be abandoned or unclaimed if the owner does not have active contact with the holder of the property in one to five years, depending on the type of property, and if the holder of the property has been unable to contact the owner of the property. A holder of unclaimed property is generally a financial institution, insurance company, publicly-traded corporation, or similar institution. Unclaimed or abandoned properties typically include contents of safe deposit boxes, wages, bank deposits, travelers checks or money orders, stock and other intangible interests in business associations, and distributions caused by certain insurance company activities.

A holder of unclaimed property is required to report annually to OST on the unclaimed property in the holder's possession. OST is required to publish in each county a legal notice of unclaimed properties reported during the previous reporting cycle (November of each year). Generally, if the OST is unable to locate the owner of the unclaimed property within three years after the receipt of the property, the property is sold. However, securities and mutual funds are generally held by OST for two years and then liquidated. In both cases, the sale proceeds are applied to the owner's account for future claims by the owners or heirs.

In January and June of each year, OST reviews its cash balances from holder reporting and securities liquidation. The amount is discounted by a reserve for future claim payouts and

administrative expenses, and the remaining funds, if any are transferred to the common school trust fund.

Currently, the unclaimed property program operates with 3.95 permanent positions and 4.0 project positions. The agency does not have in-house compliance or audit staff, and has therefore also entered into agreements with independent contractors (auditors) with experience in the identification, processing, and delivery of unclaimed property. The contracts for auditing services provide for commissions between 12% and 12.5% of the value of any cash and securities delivered to OST. OST also contracts for securities custody and management services for the OST securities portfolio. The costs of these services are based on per transaction fees.

OST has two appropriations related to the unclaimed property program. The first, s. 20.585(1)(j), is a continuing PR appropriation to receive program revenues from unclaimed property, pay claims under the program, and transfer the amounts appropriated under the second appropriation [s. 20.585(1)(k)], which is for administrative expenses, to that appropriation. The appropriation for payment of administrative expenses is an annual PR appropriation. The positions and contracted services described above are funded through the annual appropriation. Base level funding in the administrative expenses appropriation is \$1,380,600 PR.

GOVERNOR

Convert the PR appropriation for funding administrative expenses of the unclaimed property program [s. 20.585(1)(k)] from an annual to a continuing appropriation funded with all moneys transferred from the appropriation for claims.

DISCUSSION POINTS

1. Prior to 2003-04, administrative expenses of the unclaimed property program were funded through a continuing "all moneys received" PR appropriation, which was also used for the payment of claims under the program. As a result, OST was authorized to spend all program revenues received under the program to pay claims and administrative expenses. However, administrative appropriations are typically established as sum certain appropriations, which affords the Legislature more oversight than when such expenses are paid through an "all moneys received" appropriation. In order to be consistent with the general treatment of appropriations for administrative expenses, 2003 Act 33 repealed the single, continuing "all moneys received" appropriation and replaced it with the two appropriations that exist under current law.

2. In response to an increase in conversions of mutual insurance companies to publicly-held stock companies (demutualization) that was occurring at the time, Act 33 amended the unclaimed property statutes to create special reporting requirements for intangible property distributions occurring as a result of such demutualizations. [As part of the demutualization process, policy owners were offered cash or stock in exchange for their policy ownership rights in the company. Funds owed to policy owners who could not be located or did not respond were

reported to OST as unclaimed property.] The combination of the increase in demutualization of insurance companies and the state's reduction in the dormancy period (the period over which property is not yet considered unclaimed) for associated securities property have accelerated reporting and delivery of cash and securities to OST in recent years.

3. In addition, under 2005 Act 400, the dormancy period for stock or other intangible ownership interests of a business association was reduced from five years to three years, effective May 25, 2006. OST expects this law change to further contribute to larger securities remittances and corresponding increases in agency activities such as recording stock shares, confirming delivery to the custodial bank used by the unclaimed property program, and reconciling the stock and mutual fund portfolios.

4. The following table shows the value of cash and shares of securities reported under the unclaimed property program during each year from 2002-03 through 2006-07 (the 2006-07 figures are year-to-date as of early April). While the largest cash value was in 2003-04 (the result of two large insurance companies demutualizing), the general trend has been toward increasing amounts of cash and securities.

Unclaimed Property Program -- Reports of Cash and Securities

	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07*</u>
Cash	\$23,816,000	\$49,971,000	\$25,477,000	\$36,151,000	\$37,429,000
Shares of Securities	577,857	1,067,023	1,060,769	285,807	5,760,641

*As updated by OST on April 6, 2007.

5. As noted, OST presently contracts with outside vendors for help in the identification and recovery of unclaimed property. The payments to such vendors are made under the supplies and services budget under the annual PR appropriation for administrative expenses of the unclaimed property program described under current law.

6. According to OST, since the appropriation for administrative expenses of the unclaimed property program became an annual appropriation in 2003-04, contractors fees have represented between 73% and 97% of total expenditures on supplies and services. The amounts needed for such services are related to the volume and value of unclaimed property reported and serviced through such contractors and custodians.

7. Under the Committee's 14-day passive review process, OST has requested and received supplemental funding to cover the cost of such expenditures in 2003-04, 2004-05, and 2006-07. No supplemental funding was requested in 2005-06. However, 2005 Act 25 had included

a one-time significant increase in such funding for 2005-06 for the increased costs expected as a result of demutualization. The table below provides the following information related to the supply and services allocation for the unclaimed property program for fiscal years 2003-04 through 2006-07: (a) the original Chapter 20 appropriation; (b) additional sums authorized through the 14-day passive review process; and (c) the total authorization for the fiscal year. In addition, for 2003-04 through 2005-06, the final amounts expended in the fiscal year are shown.

Unclaimed Property Program -- Amounts Budgeted and Expended on Supplies and Services

	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>
Chapter 20	\$950,400	\$967,900	\$5,029,000	\$967,300
Additional Allotment	<u>7,021,900</u>	<u>973,498</u>	<u>0</u>	<u>3,370,000</u> *
Total Authorization	\$7,972,300	\$1,941,398	\$5,029,000	\$4,337,300
Total Expended	\$7,729,359	\$1,941,326	\$4,572,701	

*Of the \$3,370,000 in additional authority provided, \$2,666,700 was allocated to the supply and services line of the appropriation and \$703,300 was placed in OST's unallotted reserve line to be released by the State Budget Office upon OST's receipt of additional vendor invoices.

8. According to OST, the amounts needed to pay invoices from vendors for auditing services can not be reliably predicted ahead of time, as such amounts depend on the volume and value of unclaimed property reported and serviced by the vendors and OST first learns of the amounts when the invoices are received at the time the property is reported.

9. In order to avoid the necessity of regularly requesting supplemental funding through the Committee's 14-day passive review process, which can cause significant delays in OST's ability to pay outstanding invoices for services already received, the Governor's proposal would convert the annual appropriation for administrative expenses to a continuing appropriation equal to all moneys transferred from the appropriation for claims. As drafted, the proposed modification would result in a circular reference between the unclaimed property program's two appropriations. The current continuing claims appropriation [s. 20.585(1)(j)], which the bill would not modify, would still be for the purpose of paying claims and to transfer the amounts appropriated under s. 20.585(1)(k) for administrative expenses (underline added for emphasis). Section 20.585(1)(k), as modified under the bill, would reference moneys transferred from s. 20.585(1)(j) for administrative expenses. Each appropriation would refer to amounts based on the other appropriation. According to the drafting attorney at the Legislative Reference Bureau, the language in the bill is incorrect and should be modified.

10. To eliminate the circular reference and achieve the intent of allowing OST to meet its contractual obligations to pay vendors in a timely fashion, another approach would be to: (a)

change s. 20.585(1)(k) to a continuing appropriation equal to all moneys transferred from s. 20.585(1)(j), as provided under the bill; and (b) in addition, modify s. 20.585(1)(j) to specify that it transfer to the other appropriation the amounts required to pay administrative expenses incurred in administering Chapter 177, as determined by the Secretary of the Department of Administration. Under this option, the administration could authorize expenditures above the amounts appropriated for administrative costs as needed, without OST having to request supplement funding through the s. 16.515 process. This option would enhance OST's ability to pay vendors more promptly when property recoveries by such vendors on behalf of the state are higher than anticipated, without the circular reference that exists in the proposal as drafted.

11. For a continuing appropriation, other than a sum certain appropriation, current law requires the dollar amounts shown in the statutory appropriation schedule to represent the most reliable estimates of the amounts which will be expensed during any fiscal year. The estimates included in the bill for the unclaimed property program's administrative expenses reflect estimated supplies and services expenses of \$967,300 in each year. As described above, based on the unpredictability of vendor invoices, it is difficult to reliably estimate supplies and service expenses. However, as such expenses have ranged from \$1.9 million to \$7.7 million in recent years and are estimated at \$4.3 million in 2006-07, the estimates for administrative expenses included under the bill appear to be too low and should be increased. For example, the estimate for administrative expenses could be increased by \$3,532,700 PR in each year to allocate \$4,500,000 to the line for supplies and services. If actual administrative costs exceeded these estimates, the Secretary of DOA could authorize additional expenditure authority as needed (based on the recommended modification to the Governor's proposal described above). But the estimates reflected in the schedule would be likely to more closely approximate actual expenditures, based on recent spending patterns.

12. Another option would be to maintain the appropriation as an annual appropriation, but to increase the supplies and services allotment. Unlike the Governor's proposal, under this option, if supplemental funding were still needed, OST would have to request additional funds through the Committee's 14-day passive review process.

13. If there is no modification in the appropriation for administrative expenses, OST would continue to have the option of requesting supplemental funding for additional administrative expenses for payments to vendors through the Committee's 14-day passive review process. However, it is possible that continued delays in payments to vendors would negatively impact OST's ability to obtain vendor services, potentially leading to a significant reduction in the amounts recovered by the state through the unclaimed property program.

ALTERNATIVES TO BILL

1. Approve the Governor's proposal, with an additional modification that would set the amount transferred to the unclaimed property administrative expenses appropriation equal to the amounts required to administer the program, as determined by the Secretary of DOA. In addition,

increase estimated expenditures under the administrative appropriation by \$3,532,700 PR in each year to more accurately reflect recent expenditures.

ALT 1	Change to Bill Funding	Change to Base Funding
PR	\$7,065,400	\$7,065,400

2. Eliminate the Governor's proposal and increase funding for the supplies and service line of the administrative appropriation by \$3,532,700 PR in each year. Under this alternative, the annual appropriation for administrative expenses would be the same as the reestimated levels of administrative expenses under the Governor's proposal.

ALT 2	Change to Bill Funding	Change to Base Funding
PR	\$7,065,400	\$7,065,400

3. Delete provision. Under this alternative, it is likely that OST would have to request supplemental funding for additional administrative expenses for payments to vendors through the Committee's 14-day passive review process.

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