

Surviving an Escheatment Audit

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Your company has received an audit notice and has undertaken the arduous task of preparing for an unclaimed property audit. First, you assembled an internal group which includes your legal counsel and serves as your "internal audit defense team" or "The Team." The Team performed an internal assessment of potential liability and identified weak compliance points. It also mitigated liability where possible and devised a plan for managing the audit. Then, your company's legal counsel and/or third party audit defense consultants worked with the auditors to retrieve a nondisclosure agreement and to define the scope of the audit in terms of the number of states involved and the size of the "look back" period.

The audit opening conference is not scheduled until next week. It's now the relative calm before the storm. What should you expect from the opening conference and beyond?

The Opening Conference

The opening conference sets the stage for the entire audit. The lead auditor will explain the procedures to be used in the audit, the audit timeline and the state(s') expectations. The auditor may also provide a preliminary work plan and will query company staff about record availability. An initial document request list may be presented by the auditor. Alternatively, the document request may have been provided prior to the opening conference and be a topic of discussion during the conference. The initial document request will ask for such items as corporate history, reporting history of all entities in the audit scope, policies and procedures, bank statements and reconciliations, and a list of third party disbursement providers. Of course, administrative issues such as work space for "on-site" audit work will also be discussed during the conference.

Beyond The Opening Conference

The auditors' objective is to determine if the company is in compliance with state unclaimed property laws and the extent of any liability for non-compliance and/or inaccurate or incomplete compliance. To assess compliance, the auditor will review disbursement account activity, periodic accounting transactions (accounting data such as journal entries and

ledgers), and written documentation including procedures. Further, the auditor will interview key company personnel, make computations, and analyze data trends, etc. Throughout this process the auditor will document in work papers the company's internal policies and procedures and will evaluate the strengths and weaknesses of the controls.

A chief component of the auditors' work involves gathering evidence to use in making audit conclusions/determinations. In some instances, auditors representing the company's state of incorporation(s) may have to review recent documentation and use it as "evidence" for making extrapolations pertinent to time periods for which data does not exist. These "extrapolations" or "estimates" are often a part of the audit findings and liability assessment.

Estimates and Sampling

One of the most difficult issues in unclaimed property audits today is the appropriateness and accuracy of liability estimates based on samples used when records are not available for specific time periods or are too voluminous to review from a practical standpoint. The appropriate sample should have a low risk of error and high risk of precision.

Further, the validity of the sample can come into question for other reasons as well. The data used to extrapolate from may not be representative of the actual data as it may not involve the same type of transactions, payees, etc. Another problem is that the sample may have been drawn from a particular group of items that had a significantly higher rate of outstanding items. The company should be directly involved in drawing the sample and the auditors should explain how the results will be used in an extrapolation before the company expends resources in researching the sampled items.

Audit Matriculation Suggested Practices

The following are suggested practices for companies during the pendency of the audit:

- Stay in communication with the auditors during the audit process. Open communication may permit the company to provide data to contradict the auditors' initial assumptions regarding liability and prevent adverse audit findings.
- Request that the auditors provide a description of their sampling and extrapolation methods and, if necessary, request that the auditors consider an alternative sample or method.
- Document delivery of information provided to auditors.

- Record and copy all records that the auditors maintain for work papers.
- Request a "ball park" date for the auditors to provide their preliminary findings/analysis.

Near the end of the audit the company will be presented the auditors' preliminary findings/analysis. The company's objective should be to eliminate any possible inaccurate or misrepresentative findings before this analysis is presented. In many situations, this can be achieved by maintaining communication with the auditors, understanding the procedures to be used, and by ensuring that the procedures are sound and any samples are representative.

Next Month: Closing the Audit

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