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Unwrapping Escheat: Unclaimed Property Laws and Gift Cards

Sean M. Diamond

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UNWRAPPING ESCHEAT: UNCLAIMED PROPERTY LAWS AND GIFT CARDS

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INTRODUCTION

In the wake of the economic crisis, state budgets have been devastated by substantial decreases in revenue.¹ A traditional source for raising revenue is increased taxes, but raising taxes carries a political stigma legislators prefer to avoid.² Instead of (or in addition to) raising taxes, states often seek alternative sources of revenue through their unclaimed property laws.³ Unclaimed property laws incorporate the doctrine of escheat, which entitles a state to take custody of property that has remained unclaimed by its owner for a designated period of time.⁴ In the past twenty years, states have expanded their escheat laws and increased collection efforts to capture more unclaimed property as an alternative source of revenue.⁵ An example of this trend are states' attempts to capture the remaining value on gift cards, which independently are often small amounts but, in the aggregate, constitute a substantial sum ripe for the taking.

For the past four years, gift cards have been the most requested winter holiday item.⁶ A 2010 survey shows that consumers planned to spend an average of over \$145 per person on gift cards during the winter holiday season alone, for an estimated total of \$24.78 billion.⁷ Figures for yearly gift card

¹ See Leslie Eaton, *More States Look to Raise Taxes*, WALL ST. J., Apr. 9, 2009, at A4 (“A free fall in tax revenue is driving more state lawmakers to turn to broad-based tax increases in a bid to close widening budget gaps.”).

² See *id.* (“Raising taxes is a perilous proposition for lawmakers . . .”).

³ Suellen M. Wolfe, *Escheat and the Concept of Apportionment: A Bright Line Test to Slice a Shadow*, 27 ARIZ. ST. L.J. 173, 173 (1995); see also, e.g., Keith M. Phaneuf, *Unclaimed Properties Give State Budget a Holiday Boost*, CONN. MIRROR (Dec. 17, 2010), <http://www.ctmirror.org/story/8738/unclaimed-properties-give-state-budget-holiday-boost> (projecting \$92 million in revenue from unclaimed property for 2010, likely turning Connecticut's projected \$18 million deficit into a surplus).

⁴ True escheat laws are limited in application to real and tangible personal property. These laws transfer an absolute title to the state when the owner dies without heirs. However, this Comment uses the term *escheat* in the context of unclaimed property laws, which entitle the state to take custody of intangible personal property that has remained unclaimed for a designated period of time. The phrases *escheat laws* and *unclaimed property laws* are used interchangeably unless otherwise noted.

⁵ See Diann L. Smith & Matthew P. Hedstrom, *Will Unclaimed Property Prove an Irresistible Well?*, SUTHERLAND, 1 (June 4, 2009), <http://www.sutherland.com/files/News/9508e3c1-a85a-433c-b0cb-0bfd8d13f054/Presentation/NewsAttachment/ded2153e-872a-4b88-9101-11dd0925870a/Article6.4.09.pdf> (“The reality, however, is that if states change unclaimed property laws with the purpose of obtaining more property or obtaining the property faster, the *raison d'être* of those laws also becomes abandoned.”).

⁶ Press Release, Nat'l Retail Fed'n, Gift Givers Listening to Recipients as Gift Card Spending Expected to Rise (Nov. 17, 2010), available at http://www.nrf.com/modules.php?name=News&op=viewlive&sp_id=1033.

⁷ NAT'L RETAIL FED'N, CONSUMER INTENTIONS AND ACTIONS SURVEY 3 (2010), available at http://www.nrf.com/modules.php?name=Documents&op=showlivedoc&sp_id=5703.

spending are upwards of \$65 billion, approximately 10% of which goes unredeemed.⁸

This Comment argues that state escheat laws should not apply to gift cards because the traditional justifications for escheat are inappropriate, and because current ambiguous and antiquated legislation deters innovation that would otherwise benefit consumers and retailers alike. Gift cards also serve as an ideal example of the inadequacy of the current standard for identifying when a state has the exclusive right to escheat property. There are perplexingly wide variations among state unclaimed property laws, but the gift card market is national and consequently requires at least some national uniform doctrine, as provided by federal law. The United States Supreme Court has had multiple opportunities to provide a federal solution but has strictly adhered to a bright-line general rule rather than considering the significant nuances of unclaimed property laws. Instead, a federal resolution will depend on congressional action, as it has in the past.

Part I of this Comment provides a background discussion of gift cards' rise to prominence and their distinguishable features. It continues by tracing the roots of escheat and unclaimed property laws from feudal England to modern American Uniform Acts. Part II argues that unclaimed property laws should not apply to gift cards for at least three reasons. First, traditional justifications for unclaimed property laws do not support escheat of gift cards. Second, escheat of gift cards violates the derivative rights doctrine, which limits the rights of the state to those rights the owner was entitled to. And third, current escheat laws inadequately account for recent developments in gift cards that yield substantive, unanticipated consequences.

Part III follows the historical development of Supreme Court jurisprudence concerning conflicting claims to unclaimed property by multiple states, culminating in the current dual-priority structure, as declared in *Texas v. New Jersey*.⁹ Under *Texas*, the state of the owner's last known address has primary priority to the unclaimed property.¹⁰ However, if that state does not have legislation addressing the property in question, or if the owner's last address is unknown, then a second-priority rule takes effect.¹¹ The second-priority rule

⁸ See Erica Alini, *Governments Grab Unused Gift Cards*, WALL ST. J., June 30, 2009, at A3.

⁹ 379 U.S. 674 (1965).

¹⁰ *Id.* at 681–82.

¹¹ *Id.* at 682.

asserts that the holder's¹² state of incorporation has the authority to claim the property, subject to satisfaction of the first-priority rule at some later time.¹³

Part IV argues that the dual-priority structure is ill suited for the specific issues concerning gift cards because the first-priority rule will *never* apply when the owner's identity is necessarily unknown. Strict adherence to the dual-priority structure creates an inequitable windfall to a minority of states, such as New York and Delaware, where a disproportionate majority of businesses are incorporated. At the outset, there appear to be three possible avenues for refining the dual-priority structure: the states, the Supreme Court, or Congress. However, Congress is the only real option because the states would be preempted from resolving this problem, and the Supreme Court is unwilling to tailor its holding on a case-by-case basis. Therefore, Part V argues that Congress should pass specific legislation exempting gift cards from unclaimed property laws. This blanket exemption represents the best possible solution for a rapidly developing industry that was never intended to be included under unclaimed property laws.

I. BACKGROUND

This Part lays out the background of gift cards and escheat laws. Section A focuses on those unique characteristics of gift cards that present difficulties for unclaimed property laws. It distinguishes gift cards from other types of stored-value cards and gift certificates. Finally, this section highlights the benefits that gift cards offer consumers and retailers. Section B traces the development of escheat laws from their common law roots to the development of the modern American Uniform Acts.

A. *Gift Cards*

Gift cards have become incredibly popular since their inception in the mid-1990s.¹⁴ Consumers spend about \$65 billion on gift cards each year, of which \$6.8 billion goes unredeemed.¹⁵ The unredeemed value is commonly referred

¹² The holder is the person or entity in possession of the property that is obligated to hold the property for the benefit of the owner. See UNIF. UNCLAIMED PROP. ACT § 1(6), 8C U.L.A. 97 (2001) [hereinafter 1995 UNIF. ACT].

¹³ *Texas*, 379 U.S. at 682.

¹⁴ See Julia S. Cheney & Sherrie L.W. Rhine, *Prepaid Cards: An Important Innovation in Financial Services*, 52 CONSUMER INT. ANN. 370, 370 (2006).

¹⁵ Alini, *supra* note 8.

to as breakage.¹⁶ Gift cards are just one form of prepaid cards. A prepaid card, also known as a stored-value card (SVC), is a piece of plastic resembling a credit card that represents value already paid to the holder and that may be redeemed at a later time by the owner.¹⁷ Unlike other SVCs, gift cards are generally redeemable for merchandise only, and the holder is rarely aware of the recipient's identity.¹⁸

Further, there is an array of gift cards with varying features.¹⁹ Generally, gift cards are classified under one of two categories: closed-loop cards or open-loop cards.²⁰ Closed-loop cards are purchased directly from the retailer for fixed amounts. The accounts are directly maintained by the retailer, are redeemable at that particular retailer only, and constitute the bulk of gift card sales by number and total value.²¹ Examples of closed-loop cards include those offered by Starbucks and Best Buy.²² Conversely, open-loop cards²³ are issued by a financial institution. The accounts are maintained across debit or credit card networks and may be redeemed anywhere the supported debit or credit card is accepted.²⁴ Examples of open-loop gift cards include those offered by American Express, Visa, and MasterCard.²⁵ Additionally, gift cards in either category have various features, including the ability to reload the card

¹⁶ Phillip W. Bohl et al., *Prepaid Cards and State Unclaimed Property Laws*, 27 FRANCHISE L.J. 23, 23 (2007).

¹⁷ Mark Furletti, *Prepaid Card Markets & Regulation 2* (Fed. Reserve Bank of Phila., Payment Cards Center Discussion Paper No. 04-01, 2004), available at http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2004/Prepaid_022004.pdf. Other forms of prepaid cards include travel cards, payroll cards, and teen cards. *Id.* However, this Comment's focus is limited to gift cards.

¹⁸ See Diane Green-Kelly, *Gift Certificate and Gift Card Programs: The State Law Quagmire*, 23 FRANCHISE L.J. 211, 213 (2004). These two traits are particularly significant and troublesome for the current structure of unclaimed property laws. See *infra* Part II. Although gift cards are redeemable for merchandise only, state unclaimed property laws convert the limited right to merchandise into a greater right to cash, but this violates the derivative rights doctrine by granting a greater right to the state than the owner ever possessed. See *infra* Part II.B. A state's power to take custody of unclaimed property is primarily justified by the argument that the state is in a better position than the holder to reunite the owner with her property, but this justification falls flat in a market where the owner's identity is never known. See *infra* Part II.A.

¹⁹ Bohl et al., *supra* note 16, at 23.

²⁰ Philip Keitel, *The Laws, Regulations, Guidelines, and Industry Practices That Protect Consumers Who Use Gift Cards 2* (Fed. Reserve Bank of Phila., Payment Cards Center Discussion Paper No. 08-07, 2008), available at <http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2008/D2008JulyGiftCard.pdf>. For a discussion of innovations that have resulted in hybridized gift cards that may be classified as semi-closed or semi-open, see generally Furletti, *supra* note 17, at 4-7.

²¹ Furletti, *supra* note 17, at 2; Keitel, *supra* note 20, at 2.

²² Keitel, *supra* note 20, at 2.

²³ Open-loop gift cards are sometimes referred to as network-branded prepaid cards. See *id.* at 3.

²⁴ *Id.* at 2-3.

²⁵ *Id.* at 3.

with additional funds, options for replacement of lost or stolen cards, and expiration dates or dormancy fees.²⁶

Although somewhat similar, gift cards are distinguishable from gift certificates in a number of significant ways.²⁷ First, retailers need not reimburse consumers in cash for any unredeemed value because gift cards are able to store the card's value across multiple transactions.²⁸ Second, many gift cards may be reloaded with additional funds thanks to their value-storing capability.²⁹ Third, gift cards better protect against fraud (they are not easily counterfeited) and theft (they are not activated until the time of sale).³⁰ Finally, gift cards are better equipped to track consumer usage for marketing purposes.³¹

The benefits of gift cards extend to both consumers and retailers. Gift cards offer consumers convenience by reducing transaction costs and are often more desirable as gifts because they retain the utility of cash but convey a greater degree of thoughtfulness.³² Gift cards benefit retailers by increasing customer loyalty and sales volume, reducing credit risk, and decreasing time spent at the point of sale.³³

B. Escheat and Unclaimed Property Laws

To better understand the purpose of modern unclaimed property laws, the development of the dual-priority structure for competing interstate claims, and the legitimacy of a third-priority rule, this section will first address the origin of unclaimed property laws, and second, the creation of various Uniform Acts. This section concludes by arguing that the underlying justifications of unclaimed property laws do not support states' claims on gift card breakage.

²⁶ Bohl et al., *supra* note 16, at 23.

²⁷ Furletti, *supra* note 17, at 2–3.

²⁸ *Id.* at 3.

²⁹ *See, e.g., Card FAQs*, STARBUCKS COFFEE CO., <http://www.starbucks.com/customer-service/faqs/card> (last visited Mar. 7, 2011).

³⁰ Furletti, *supra* note 17, at 3.

³¹ *Id.*

³² *See* The Mktg. Workshop, Inc., Marketing Intelligence Through Research: Adult Gift Card Study 2007, at 36–38 (2007) (PowerPoint presentation) (on file with the Emory Law Journal) (surveying reasons that respondents purchased gift cards for themselves or others).

³³ Furletti, *supra* note 17, at 3.

1. *Common Law Roots and Subsequent Departure*

American unclaimed property laws are rooted in the feudal English common law doctrines of escheat and *bona vacantia*.³⁴ Under the doctrine of escheat, the real property of a tenant who died without heirs would revert back to the feudal lord or Crown.³⁵ Similarly, the doctrine of *bona vacantia* prescribed that abandoned personal property would transfer to the Crown.³⁶ Under escheat the Crown's claim was based on its status as the ultimate owner of all real property, whereas under *bona vacantia* the Crown simply had a greater claim to personal property than all but the rightful owner.³⁷

Following the Revolutionary War and formation of the United States, the states adopted English common law regarding escheat and *bona vacantia*.³⁸ However, the Americanization of these two doctrines quickly departed from their feudal foundations and eventually merged into a single doctrine of escheat, which encompassed both real and tangible personal property.³⁹

Under the American doctrine, instead of reverting to the Crown, real and tangible personal property transfers in title to the state, provided the state has enacted specific legislation.⁴⁰ Although the sovereignty of the Crown was disseminated among the various states, determining the particular state to which real and tangible personal property should escheat is relatively easy. The state in which the property is physically located—the *situs*—has the exclusive power to escheat.⁴¹ In other words, for a state to have the power to escheat real or tangible personal property, the state must have specific

³⁴ Susan T. Kelly, Note, *Unclaimed Billions: Federal Encroachment on States' Rights in Abandoned Property*, 33 B.C. L. REV. 1037, 1041 (1992).

³⁵ Andrew W. McThenia, Jr. & David J. Epstein, *Issues of Sovereignty in Escheat and the Uniform Unclaimed Property Act*, 40 WASH. & LEE L. REV. 1429, 1430 (1983).

³⁶ *Id.* at 1431.

³⁷ *Id.* at 1430–31 nn.3–4.

³⁸ 1 DAVID J. EPSTEIN, UNCLAIMED PROPERTY LAW AND REPORTING FORMS § 1.04 (Matthew Bender rev. ed. 2010).

³⁹ *Id.* (“Like most seeds transported to foreign soil and a different climate, the offspring that flourished was far different from the original stock.”); see also Note, *Origins and Development of Modern Escheat*, 61 COLUM. L. REV. 1319, 1327 (1961) (“Modern statutes thus perform dual functions, continuing the traditions of both *bona vacantia* and common law escheat.”).

⁴⁰ EPSTEIN, *supra* note 38, § 1.04; see also *Conn. Mut. Life Ins. Co. v. Moore*, 333 U.S. 541, 546 (1948) (“The state may more properly be custodian and beneficiary of abandoned property than any person.”). Although the United States Constitution does not expressly grant the federal government the power to escheat, there have been particular circumstances where a federal power to escheat has been upheld. See, e.g., *United States v. Oregon*, 366 U.S. 643 (1961) (upholding a federal statute that enables the federal government to claim personal property of a veteran who dies intestate in a Veterans' Administration Hospital).

⁴¹ *Texas v. New Jersey*, 379 U.S. 674, 677 (1965).

legislation covering the property in question, and the property must be physically located within the state's territorial borders.

Modern American development of unclaimed property laws, however, significantly departed from its English common law roots.⁴² Courts and state legislatures expanded the subject matter of escheat to include unclaimed intangible personal property.⁴³ Unlike the English common law of escheat and *bona vacantia*, which vested absolute title to the Crown, American unclaimed property laws are generally custodial in nature⁴⁴—the state merely holds the unclaimed property in perpetuity until the rightful owner asserts a claim to it.⁴⁵ A significant consequence of this custodial nature is the derivative rights doctrine, which provides that the rights of the state as to the unclaimed property are derived from the rights of the owner.⁴⁶ In other words, the state stands in the shoes of the owner and has no greater rights to the unclaimed property than did the owner.⁴⁷

Further, unclaimed property laws differ from true escheat laws insofar as unclaimed property laws are based on abandonment rather than intestate succession and apply primarily to intangible personal property.⁴⁸

Similar to American escheat of real and tangible personal property, a state's power to take custody of unclaimed intangible personal property depends on

⁴² Kelly, *supra* note 34, at 1043; *cf.* 1995 UNIF. ACT, *supra* note 12, prefatory note, 8C U.L.A. at 89 (“[T]he State does not take title to unclaimed property, but takes custody only, and holds the property in perpetuity for the owner.”). However, a few states have enacted unclaimed property laws that are truly escheat statutes. Kelly, *supra* note 34, at 1043–44 & n.60 (citing IND. CODE ANN. § 32-9-1-36 (LexisNexis 1991); N.H. REV. STAT. ANN. § 471-C:30 (1990)).

⁴³ EPSTEIN, *supra* note 38, § 1.04; *see also* *Cunnius v. Reading Sch. Dist.*, 198 U.S. 458 (1905) (finding that interest payments were subject to unclaimed property laws). However, prior to the first Uniform Act in 1954, only ten states had enacted comprehensive unclaimed property legislation. Michael Houghton et al., *Unclaimed Property*, 74-2d C.P.S. (BNA) § II(B)(1) (2003).

⁴⁴ *See* 1995 UNIF. ACT, *supra* note 12, prefatory note, 8C U.L.A. at 89.

⁴⁵ Kelly, *supra* note 34, at 1043; *see also* 1995 UNIF. ACT, *supra* note 12, prefatory note, 8C U.L.A. at 89.

⁴⁶ I ANTHONY L. ANDREOLI & J. BROOKE SPOTSWOOD, *GUIDE TO UNCLAIMED PROPERTY AND ESCHEAT LAWS* § 3.05 (2d ed. 1998); *see also* Houghton et al., *supra* note 43, § VI(C).

⁴⁷ Ethan D. Millar & John L. Coalson, Jr., *The Pot of Gold at the End of the Class Action Lawsuit: Can States Claim It as Unclaimed Property?*, 70 U. PITT. L. REV. 511, 516 (2009); *see also* Houghton et al., *supra* note 43, § VI(C). However, there are some exceptions to this fundamental principle. For example, although a statute of limitations may circumscribe an owner's ability to claim her property from a holder under some circumstances, section 19(a) of the 1995 Act precludes such a statute of limitations from preventing a state's claim against a holder. *See* 1995 UNIF. ACT, *supra* note 12, § 19(a), 8C U.L.A. at 134–35; ANDREOLI & SPOTSWOOD, *supra* note 46, § 7.03.

⁴⁸ Kelly, *supra* note 34, at 1044. Unclaimed property laws extend to limited types of tangible personal property as well, such as the contents of safe-deposit boxes. *See* 1995 UNIF. ACT, *supra* note 12, § 3, 8C U.L.A. at 110.

whether the state has specific legislation covering the property in question. However, the primary difficulty in determining a state's sovereignty over intangible personal property is that, by its nature, intangible personal property cannot be located on a map. To resolve this difficulty, states and courts later ventured to construct a standard for determining a fictional situs for unclaimed property.⁴⁹

2. *Uniform Unclaimed Property Acts*

Although true escheat laws present little difficulty in determining the situs of the property in question, the opportunity for states to capitalize on property from owners who die intestate occurs relatively infrequently.⁵⁰ As states began to realize there were more lucrative opportunities in unclaimed intangible personal property,⁵¹ aided by the Supreme Court's general willingness to uphold state unclaimed property laws,⁵² legislation increased among the states to capture unclaimed property as a form of nontax revenue.⁵³ However, the legislation varied substantially from state to state and was "neither well-organized nor well-integrated."⁵⁴ In 1954, the National Conference of Commissioners on Uniform State Laws (NCCUSL) drafted the Uniform Disposition of Unclaimed Property Act (the 1954 Act) to resolve the escalating confusion among the states.⁵⁵

Since the 1954 Act, the NCCUSL has adopted three subsequent versions of the Uniform Act.⁵⁶ The 1954 Act was revised in 1966,⁵⁷ and in 1981 the NCCUSL proposed the Uniform Unclaimed Property Act (the 1981 Act),⁵⁸

⁴⁹ McThenia & Epstein, *supra* note 35, at 1434–35; *see also infra* Part III.

⁵⁰ *See* Wolfe, *supra* note 3, at 173.

⁵¹ Note, *supra* note 39, at 1330.

⁵² McThenia & Epstein, *supra* note 35, at 1436.

⁵³ Wolfe, *supra* note 3, at 190.

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ NETWORK BRANDED PREPAID CARD ASS'N, NBPCA WHITE PAPER—ABANDONED PROPERTY LAWS AND NETWORK BRANDED PREPAID CARDS: QUESTIONS AND CONCERNS RAISED WHEN TRYING TO FIT CARDS INTO THE EXISTING ABANDONED PROPERTY LEGAL FRAMEWORK 3–5 (2009).

⁵⁷ The revisions were made particularly to address issues with money orders and traveler's checks. *Id.* at 4.

⁵⁸ The 1981 Act superseded the previous versions and codified the holding in *Texas v. New Jersey*, 379 U.S. 674 (1965), regarding the priority structure of conflicting interstate claims to abandoned property. Houghton et al., *supra* note 43, § III(C); *see also infra* Part III. Additionally, the 1981 Act was the first version to expressly add gift certificates to the definition of intangible property. NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 4.

which was subsequently revised in 1995 (the 1995 Act).⁵⁹ The majority of states have adopted some version of the Uniform Act, subject to modification.⁶⁰ All versions are custodial⁶¹ and exclusively cover intangible personal property.⁶²

The Acts apply when property is “presumed abandoned.”⁶³ The 1995 Act includes a general definition of “property,” whereas the earlier versions devised specific rules catered to particular holders.⁶⁴ Various categories of property have differing dormancy periods, after which they are presumed abandoned.⁶⁵ The holder of such property—the entity that is obligated to hold the property on account of the owner—must file a report with the state administrator listing the type of property and specific information about the owner, if recorded.⁶⁶ Once the dormancy period has transpired, the state takes possession of the property and must take affirmative steps to notify the owner.⁶⁷ After a specified period of time, the state sells the unclaimed property and deposits the proceeds into the general fund or some other state fund.⁶⁸ Finally, the rightful owners, including heirs and devisees, may claim the funds at any future point.⁶⁹

The stated objectives of the Acts include protection, convenience, accessibility, fairness, and assurance that the public benefits from the use of unclaimed property.⁷⁰ The Acts protect the owner’s property until it can be

⁵⁹ Ellen P. Aprill, *Inadvertence and the Internal Revenue Code: Federal Tax Consequences of State Unclaimed Property Laws*, 62 U. PITT. L. REV. 123, 134 (2000). The 1995 Act diverged from the previous versions in organization and effect, refined the definition of “holder” in response to *Delaware v. New York*, 507 U.S. 490 (1993), and shortened dormancy periods for gift certificates among other types of property. NETWORK BRANDED PREPAID CARD ASS’N, *supra* note 56, at 5; *see also* Aprill, *supra*, at 134.

⁶⁰ *See* NETWORK BRANDED PREPAID CARD ASS’N, *supra* note 56, at 3.

⁶¹ 1995 UNIF. ACT, *supra* note 12, prefatory note, 8C U.L.A. at 89.

⁶² *Id.* § 1 cmt., 8C U.L.A. at 100. *But see supra* note 48 (noting that the contents of safe-deposit boxes are subject to escheat).

⁶³ *See* 1995 UNIF. ACT, *supra* note 12, §§ 2, 4, 8C U.L.A. at 102, 111; Aprill, *supra* note 59, at 134.

⁶⁴ Houghton et al., *supra* note 43, § IV(A). However, all versions include a catch-all provision. *See id.* § IV(A) n.4; *accord* 1995 UNIF. ACT, *supra* note 12, § 2(a)(15), 8C U.L.A. at 103 (providing a five-year dormancy period for “all other property”).

⁶⁵ *See* Aprill, *supra* note 59, at 134–35 (“For example, wages and other compensation for personal services are presumed abandoned one year after the compensation becomes payable.”). The dormancy periods were shortened in the 1981 Act, Houghton et al., *supra* note 43, § III(C), and again in the 1995 Act, Aprill, *supra* note 59, at 135.

⁶⁶ Aprill, *supra* note 59, at 134–35.

⁶⁷ *Id.* at 135–36.

⁶⁸ *Id.* at 136.

⁶⁹ *Id.*

⁷⁰ NETWORK BRANDED PREPAID CARD ASS’N, *supra* note 56, at 3.

reclaimed.⁷¹ They create convenience by facilitating a single location for rightful owners to discover and assert a claim to their property.⁷² The Acts uphold fairness by preventing private holders of unclaimed property from receiving an unjust windfall.⁷³ Finally, the Acts aim to prevent economic waste by redirecting unclaimed property back to the public.⁷⁴

II. WHY UNCLAIMED PROPERTY LAWS SHOULD NOT APPLY TO GIFT CARDS

This Part argues that unclaimed property laws should not encompass gift cards within their subject matter.⁷⁵ Section A argues that the traditional justifications for unclaimed property laws fall short when applied to gift cards. For example, the primary objective of unclaimed property laws is to reunite the owner with her property, and the laws assume that the state is in a better position to facilitate recovery than the person or entity in possession of the property. However, because states and retailers do not know the identity of the ultimate recipient of gift cards, the state is no better equipped than the retailer to reunite gift cards with their anonymous owners. Section B argues that unclaimed property laws that attempt to escheat the full face value of gift cards violate the derivative rights doctrine. Section C argues that reporting procedures' complexity and unclaimed property laws' failure to clearly address gift cards create practical problems, even for businesses attempting to comply in good faith. This uncertainty will have a chilling effect on innovation in a rapidly developing industry that benefits consumers and retailers alike.

⁷¹ *Id.*

⁷² *Id.*

⁷³ *Id.* However, at least one court has noted the inherent tension between this purpose and the purpose of reuniting the property with the owner. *See Taylor v. Chiang*, No. Civ. S-01-2407 WBS GGH, 2007 WL 1628050, at *4 (E.D. Cal. June 1) (“If the purpose of the law is . . . to reunite owners with their lost or forgotten property, its ultimate goal should be to generate little or no revenue at all for the state.”), *vacated on other grounds*, 2007 WL 3049645 (E.D. Cal. Oct. 18, 2007), *aff’d in part, rev’d in part sub nom. Taylor v. Westly*, 525 F.3d 1288 (9th Cir. 2008).

⁷⁴ NETWORK BRANDED PREPAID CARD ASS’N, *supra* note 56, at 3. However some courts have reasoned that the goal of raising revenue should be minimized in light of the primary goal of reuniting owners with their property. *See Taylor*, 2007 WL 1628050, at *4; *Millar & Coalson*, *supra* note 47, at 516–17 & n.9 (citing *Am. Express Travel Related Servs. Co. v. Hollenbach*, 630 F. Supp. 2d 757 (E.D. Ky. 2009)).

⁷⁵ A majority of states have either fully or partially exempted gift cards from their escheat laws for many of the reasons discussed in this Part. The 1981 and 1995 Acts, however, encompass gift *certificates* within their subject matter. 1995 UNIF. ACT, *supra* note 12, § 1(13)(ii), 8C U.L.A. at 98; UNIF. UNCLAIMED PROP. ACT § 14, 8C U.L.A. 216 (2001) (superseded 1995) [hereinafter 1981 UNIF. ACT]. Some states have unclaimed property legislation that expressly addresses gift certificates—for example, Delaware, DEL. CODE ANN. tit. 12, §§ 1198–1199 (2010), and New York, N.Y. ABAND. PROP. LAW § 1315 (McKinney 2009), where a majority of businesses are incorporated. Under the dual-priority structure discussed below in Part III.B, these states will continue to reap substantial benefits from unclaimed gift card breakage.

A. *Traditional Justifications Fall Flat*

Although the justifications for unclaimed property laws effectively apply to most types of intangible personal property, those justifications fall flat when applied to gift cards. The primary objective of unclaimed property laws is to reunite property with its rightful owner.⁷⁶ However, the very nature of gift cards is such that neither the name nor the last known address of the ultimate recipient is ever disclosed to the holder. Consequently, states are *never* able to reunite unclaimed breakage with its anonymous owner.⁷⁷

Arguably, nothing prohibits states from requiring businesses to obtain the identity and address of the ultimate recipient of gift cards, which would resolve this informational gap.⁷⁸ However, state laws requiring businesses to obtain the ultimate recipient's personal information would be unreasonable for several reasons. Most importantly, businesses sell gift cards anonymously to protect consumer privacy concerns.⁷⁹ Requiring consumers to disclose their own personal information violates these privacy concerns, never mind requiring them to disclose the personal information of recipients. Second, mandated disclosure vitiates the benefit that gift cards create by reducing transaction costs for consumers and retailers.⁸⁰ For example, a consumer will be dissuaded from purchasing a gift card if the consumer must have on hand the recipient's personal information at the time of sale. Finally, businesses often offer optional registration⁸¹ and are better positioned than government to determine the ideal methods for such programs.

⁷⁶ See NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 3, 19.

⁷⁷ The Court in *Pennsylvania v. New York* refused to accept as a relevant concern that money orders involve a higher percentage of unknown addresses than other forms of unclaimed property. 407 U.S. 206, 214–15 (1972). However, this may be explained by the fact that the Court believed that there were actually “a substantial number of creditors’ addresses” available. *Id.* at 215.

⁷⁸ EPSTEIN, *supra* note 38, § 9.01; see also *Delaware v. New York*, 507 U.S. 490, 509 n.12 (1993) (“[N]othing in our decisions ‘prohibits the States from requiring [debtors] to keep adequate address records.’” (second alteration in original) (quoting *Pennsylvania*, 407 U.S. at 215)). For example, New Jersey recently enacted legislation that requires SVC issuers to “obtain the name and address of the purchaser or owner of each stored value card issued or sold.” N.J. STAT. ANN. § 46:30B-42.1(c) (West 2010). Although this section of the New Jersey statute was challenged on federal constitutional grounds, the data-collection provision was initially upheld. See *N.J. Retail Merchs. Ass’n v. Sidamon-Eristoff*, No. 10-5059 (FLW), 2011 U.S. Dist. LEXIS 3911, at *24 (D.N.J. Jan. 14, 2011). However, two weeks later, the Third Circuit granted a temporary injunction enjoining enforcement of the data-collection provision. See *Order Granting Temporary Injunction*, No. 11-1141 (3d Cir. Jan. 31, 2011), available at <http://files.cecollect.com/111/1312/Order.pdf>.

⁷⁹ Alini, *supra* note 8.

⁸⁰ See EPSTEIN, *supra* note 38, § 12.31 (“The transactions which give rise to such property simply do not provide a reasonable opportunity for detailed information-gathering.”).

⁸¹ See, e.g., *Card FAQs*, *supra* note 29.

The justification of convenience (i.e., creating a single location for an owner to discover and assert a claim) fails for the same reason that the justification of protection fails. Since there is no record of the owner's name or last known address, it is impossible for an owner to discover—let alone assert a claim to—her unclaimed property. In fact, if a business offers a registration option then it will be more likely to notify an owner that she has breakage; the owner will be more likely to return to the business to redeem her balance, and possibly make additional purchases. In this situation, it is far more convenient for an owner to be notified rather than placing the burden of discovery on the owner. While many states have created websites for consumers to search for unclaimed property,⁸² such states do not go beyond this passive form of notice. Further, the procedure for asserting a claim to unclaimed property from the state may be particularly rigorous and hardly convenient.⁸³

The next two justifications—preventing unjust windfalls to private holders and redirecting unclaimed property back to the public—are equally unconvincing for related reasons. Windfalls may be understood, as one commentator argues, “as economic gains independent of work, planning, or other productive activities that society wishes to reward.”⁸⁴ True escheat laws aptly fit this definition.⁸⁵ For example, the behavior of most people to draft wills rather than to “die broke” indicates that there is some utility in distributing wealth after death.⁸⁶ This utility incentivizes people to participate in productive activities, which is desirable to society.⁸⁷ Conversely, if a person dies intestate and without heirs, the state may properly escheat the estate because this windfall capture does not create disincentives for the living to avoid working hard for the benefit of their successors.⁸⁸

⁸² See, e.g., *Unclaimed Property Program*, GA. DEP'T OF REVENUE, <https://etax.dor.ga.gov/PTD/ucp/index.aspx> (last visited Mar. 7, 2011).

⁸³ See, e.g., *Escheat—Unclaimed Property*, DEL. DIV. OF REVENUE, http://revenue.delaware.gov/unprop/unprop_search.shtml (last visited Mar. 7, 2011) (requiring submission of a “coupon” along with a copy of the claimant's driver's license, followed by subsequent submission of “additional information,” all of which takes upwards of sixteen weeks to complete).

⁸⁴ Eric Kades, *Windfalls*, 108 YALE L.J. 1489, 1491 (1999) (emphasis omitted).

⁸⁵ *Id.* at 1553–54.

⁸⁶ *Id.* at 1553. When a person dies intestate, but has heirs, the estate usually transfers to the heirs under the presumption that everyone intends to bequeath their property to relatives despite the oversight of not drafting a will. *Id.*

⁸⁷ See *id.* (“[Distributing wealth to heirs rather than annuitizing wealth during old age] indicates that making gifts upon death has great utility to most people.”).

⁸⁸ *Id.* at 1553–54.

However, when this windfall analysis is applied to the escheat of gift cards, it is apparent that gift card breakage is not actually a windfall because the breakage is returned to a more closely tailored group than the general public.⁸⁹ Businesses have invested substantially in the development of gift cards, an innovation that benefits both consumers and retailers.⁹⁰ Breakage is a direct result of the productive activities of businesses reflecting the costs of development, and therefore not a windfall that the state is entitled to capture.

Further, under the above windfall analysis, the exemption of gift cards from escheat laws is more likely to return the economic gain to the owners.⁹¹ In a competitive market, businesses that retain breakage are likely to pass on the savings to consumers, who are a smaller population than the general public, and this subgroup is more likely to encompass gift card owners and purchasers.⁹² The consumer's risk of failing to redeem the full value of gift cards is spread across a smaller and more relevant group. This reduces costs, encourages an industry that benefits society, and minimizes economic waste.⁹³

B. Converting a Right to Merchandise into a Right to Cash Violates the Derivative Rights Doctrine

Another criticism of state unclaimed property laws that apply to gift cards is based on their violation of the derivative rights doctrine, which limits the rights of the state to the rights of the owner.⁹⁴ Owners of gift cards have the limited right to exchange the value stored on the gift card for merchandise but are not entitled to exchange that stored value for cash.⁹⁵ However, states that escheat gift card breakage require the holder to turn over the cash value in lieu of merchandise. This practice effectively grants a greater right to the state than the owner ever had.⁹⁶

⁸⁹ *Cf. id.* at 1554 (“[O]ther recent innovations of the doctrine are questionable.”).

⁹⁰ *See supra* Part I.A.

⁹¹ *Cf. Kades, supra* note 84, at 1554 (analyzing the validity of escheat of unredeemed traveler's checks under a windfall analysis).

⁹² *See id.*

⁹³ *See id.*

⁹⁴ *See supra* Part I.B.1.

⁹⁵ *See supra* Part I.A.

⁹⁶ *See* Millar & Coalson, *supra* note 47, at 530 (noting that states' conversion of vouchers or coupons, which are often awarded to plaintiffs in class action settlements and are redeemable for merchandise only, into cash through escheat violates the derivative rights doctrine).

Courts have addressed this issue with conflicting results. In *Connecticut Mutual Life Insurance Co. v. Moore*,⁹⁷ the Supreme Court did not require the state to satisfy an insurance provision that required the policyholder to present proof of death because the state was acting as a conservator and it would be unreasonable to compel the state to comply with conditions that would otherwise be proper between the contracting parties.⁹⁸ Accordingly, for a state to avoid violation of the derivative rights doctrine, the limitation on the owner's right to performance must be proper, and the condition must be unreasonable for the state, as a conservator, to satisfy.⁹⁹

Arguably, requiring a state to collect merchandise from retailers would seem unreasonable. However, several courts have concluded that the state is not entitled to cash for unredeemed, merchandise-only gift certificates.¹⁰⁰ Conversely, other courts have held that states may escheat the cash equivalent for unredeemed, merchandise-only gift certificates.¹⁰¹ Even if there is no violation of the doctrine because it is unreasonable to require a state to collect merchandise, escheat of the full face value of the gift card is certainly a violation. When a consumer uses a gift card for merchandise, the value of the gift card is applied to the merchandise's retail value, while the business retains the profit from the difference between the wholesale and retail prices. Therefore, a state claiming the full value of the breakage violates the doctrine by obtaining a right to the merchandise's wholesale value instead of its lesser retail value. Section 2(7) of the 1995 Act takes this into consideration and attempts to avoid any violation by limiting the amount of escheat for merchandise-only gift certificates to 60% of the face value.¹⁰²

However, as the next section addresses, it is unclear whether gift cards even fall under the same provisions that apply to gift certificates. If gift cards

⁹⁷ 333 U.S. 541 (1948).

⁹⁸ *Id.* at 547.

⁹⁹ EPSTEIN, *supra* note 38, § 9.04.

¹⁰⁰ *E.g.*, *In re* Nov. 8, 1996, Determination of the State, Dep't of the Treasury, Unclaimed Prop. Office, 706 A.2d 1177 (N.J. Super. Ct. App. Div. 1998), *aff'd per curiam*, 722 A.2d 536 (N.J. 1999); *State v. Sperry & Hutchinson Co.*, 153 A.2d 691 (N.J. Super. Ct. App. Div. 1959); *Serv. Merch. Co. v. Adams*, No. 97-2982-III, 2001 WL 34384462 (Tenn. Ch. Ct. June 29, 2001), *appeal dismissed on other grounds*, No. M2001-01895-COA-R3-CV (Tenn. Ct. App. Jan. 14, 2002). Some commentators, however, have questioned the underlying reasoning of the holdings in these cases. *See, e.g.*, EPSTEIN, *supra* note 38, § 9.04.

¹⁰¹ *E.g.*, *State ex rel. Callahan v. Marshall Field & Co.*, 404 N.E.2d 368 (Ill. App. Ct. 1980); *Murdock v. John B. Stetson Co.*, 32 Pa. D. & C.2d 300, 1963 WL 6456 (Ct. Com. Pl. 1963).

¹⁰² 1995 UNIF. ACT, *supra* note 12, § 2(7), 8C U.L.A. at 103; *cf.* ME. REV. STAT. ANN. tit. 33, § 1953(G) (2009).

instead fall under the 1995 Act's catch-all provision,¹⁰³ which does not account for retailers' anticipated profits, then escheat of gift cards remains a violation of the derivative rights doctrine.

C. Practical Problems of Compliance

Many states' unclaimed property laws were written before the prominence of gift cards and consequently fail to provide adequate guidance for retailers while subjecting them to the risk of substantial noncompliance consequences.¹⁰⁴

While the 1995 Act includes gift certificates under its definition of property,¹⁰⁵ it does not explicitly include gift cards nor does it provide a definition of *gift certificate*. Although states will likely interpret gift cards to fall under the gift certificate category, this approach presents issues that are difficult to resolve.¹⁰⁶ For example, shoehorning gift cards into the gift certificates category leaves uncertain whether reloading a gift card with additional funds—an attribute unique to gift cards—would interrupt the running of the dormancy period or whether the dormancy period would continuously run from the date of purchase.¹⁰⁷ Businesses utilizing gift cards instead of gift certificates will have scant guidance as to whether states that exempt gift certificates from reporting will also exempt gift cards, or whether gift cards might fall under the law's catch-all provision for intangible personal property not conceived of at the time the law was written.¹⁰⁸ The period of presumed abandonment will be equally unclear when the 1995 Act states that it is three years for gift certificates, while it is five years for property that falls under the catch-all provision.¹⁰⁹

¹⁰³ See *infra* Part II.C.

¹⁰⁴ See Stephanie Cutler et al., *What Corporate America Needs to Know About Unclaimed Property: A Primer for the Business Holder*, 54 TAX EXECUTIVE 335, 337–38 (2002) (describing the risks of noncompliance with state unclaimed property laws).

¹⁰⁵ 1995 UNIF. ACT, *supra* note 12, § 1, 8C U.L.A. at 98.

¹⁰⁶ Houghton et al., *supra* note 43, § VIII(A). However, at least one state, Colorado, has concluded that gift cards fall under the catch-all provision rather than the gift certificate provision. See Status of Stored Value Cards, Including Gift Cards, Op. Att'y Gen. No. 05-01, 2005 Colo. AG LEXIS 1, at *1, *4 (Apr. 13, 2005).

¹⁰⁷ Houghton et al., *supra* note 43, § VIII(A).

¹⁰⁸ See *id.* (noting that exemptions applicable to gift certificates may not apply to gift cards).

¹⁰⁹ NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 14. Adding yet another wrinkle to the compliance problem is the enactment of the Credit CARD Act of 2009, which provides that gift cards may not expire until at least five years from the date they are issued. Pub. L. No. 111-24, sec. 401, § 915(c)(2), 123 Stat. 1734, 1753 (codified at 15 U.S.C. § 1693l-1(c)(2) (Supp. III 2009)). Consequently, issuers may be forced to report unclaimed breakage to states before gift cards have even expired under federal limits. This would increase the likelihood that businesses will later have to seek reimbursement from states when

Another difference between certificates and cards is the gift card's unique ability to store its remaining value after multiple uses, which creates uncertainty for purposes of determining what face value means.¹¹⁰ The face value of a gift certificate necessarily indicates the actual amount presumed abandoned because a certificate's single-use trait entails that the certificate has been used either in full or not at all. A gift *card* owner, however, may use all but \$10 of the gift card's \$100 face value.¹¹¹ Under the 1995 Act, which requires the holder to submit 60% of the face value, would the retailer be required to submit \$6 or \$60?¹¹² The answer remains unclear. Common sense demands that the latter amount could not possibly be correct because the holder would lose money by implementing gift cards, but a strict interpretation of the Act's language does not support this commonsense conclusion. The uncertainty is likely to dissuade many businesses from offering gift cards, particularly smaller businesses where the costs of legal consultation and risks of audit or litigation will outweigh the benefits of gift card programs.

The risks of noncompliance are substantial even for businesses that attempt in good faith to adhere to states' unclaimed property laws.¹¹³ As states have increasingly used unclaimed property laws as a source of nontax revenue, businesses have been subjected to more comprehensive state audits.¹¹⁴ Audits for unclaimed property may reach back at least ten years, and in some states as far back as fifteen to twenty years, before the expiration of the dormancy period.¹¹⁵ If the business records are incomplete or nonexistent, the auditors may use an estimation process—regarded as dubious by some commentators—to determine the principal amount of property owed.¹¹⁶ Any unreported property is then subject to an interest rate upwards of 18% per year, may incur

consumers use unexpired, but escheated gift card breakage. See *New York and New Jersey Propose Significant Unclaimed Property Amendments*, SUTHERLAND, 2 (July, 7, 2010), <http://www.sutherland.com/files/News/5d7e4f3b-c493-40c9-b372-505024d185d6/Presentation/NewsAttachment/e2eb7b96-81a4-4852-81fe-52fc6d95b249/SALT%20Alert%207.7.10.pdf>.

¹¹⁰ See NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 18 ("If there is no face amount on the prepaid card, does that mean there is no escheat obligation?").

¹¹¹ *See id.*

¹¹² *See id.* ("The law was written with a one-time-use paper gift certificate in mind and does not translate equitably to multi-use prepaid cards with a 'face value' that may have no relation to the current value.").

¹¹³ Cutler et al., *supra* note 104, at 337.

¹¹⁴ *Id.* at 336–37; cf. *Unclaimed Property Laws: Gift Card Stocking Stuffers Can Become Lumps of Coal for Unwary Retailers*, MORGAN LEWIS, 2 (Dec. 21, 2010), http://www.morganlewis.com/pubs/Tax_LF_UnclaimedPropertyLaws_21dec10.pdf (noting that Delaware often hires third-party auditors on a contingency basis).

¹¹⁵ Cutler et al., *supra* note 104, at 337.

¹¹⁶ *Id.*

monetary penalties as high as \$500 per day of noncompliance, and in some rare cases may result in criminal penalties.¹¹⁷ Additionally, noncompliance may subject businesses to federal liability for violations of the Sarbanes–Oxley Act of 2002 or Generally Accepted Accounting Principles.¹¹⁸

D. Summary

Given the lackluster justifications for applying unclaimed property laws to gift cards, the difficulties they present for the derivative rights doctrine, the lack of clarity in current state laws, and the high stakes of noncompliance, it is clear why more than half the states have exempted gift cards to some degree from their unclaimed property laws.¹¹⁹ Unfortunately, those states that continue to include gift cards in their unclaimed property laws are able to escheat gift cards even when the cards are bought or sold in states that exempt gift cards. The following Part addresses this discrepancy and what solutions there may be to amend the current structure of unclaimed property laws generally, or specifically, in the gift card context.

III. CONFLICTING INTERSTATE CLAIMS

In Parts I and II, this Comment addressed the question of *what* property should be the subject matter of unclaimed property laws and concluded that such laws should not encompass gift cards. The next question, which this Part addresses, is to *which* state does unclaimed property escheat. While determining the situs of tangible property is quite easy, it is far more difficult to identify the “situs” of intangible property, which necessarily cannot be geographically located.

This Part begins in section A by describing the Supreme Court’s initial efforts to determine which state has the power to escheat and how the Court struggled to identify the fictional situs of intangible property. Section B addresses the Court’s creation of the current system. In *Texas v. New Jersey*,¹²⁰ the Court devised the dual-priority structure whereby unclaimed property escheats to the state of the owner’s last known address. However, if

¹¹⁷ *Id.*

¹¹⁸ Houghton et al., *supra* note 43, § VII(A)–(B).

¹¹⁹ For a comprehensive summary of state—and to a lesser extent, federal—laws regarding gift cards, see *Gift Cards and Gift Certificates Statutes and Legislation*, NAT’L CONFERENCE OF STATE LEGISLATURES, <http://www.ncsl.org/default.aspx?tabid=12474> (last updated Sept. 3, 2010).

¹²⁰ 379 U.S. 674 (1965).

there is no last known address, then the unclaimed property escheats to the state of the holder's incorporation. Initially this structure was premised on efficiency and equity, and not on precedent. In subsequent cases the Court faced more complex fact situations that questioned the utility of the dual-priority structure, but the Court strictly adhered to its rule based on efficiency and precedent. However, the subsequent holdings departed from the Court's reasoning in *Texas*, which was based on equity. Ultimately, the Court indicated that it would not depart from its bright-line rule in *Texas* and effectively delegated to Congress the responsibility of making any necessary changes. The consequences of this line of cases in the gift card context will be addressed in Part IV.

A. *The Race of Diligence*

Traditionally, a state's power to escheat property was determined by whether the situs of the property was located within that state's territorial borders.¹²¹ Although identifying the situs of tangible property is relatively straightforward, difficult issues arise when attempting to locate a fictional situs for intangible property.¹²² Up until the mid-twentieth century, the bulk of unclaimed property litigation revolved around intrastate disputes regarding states' power to escheat.¹²³ However, the likelihood of conflicting state claims became inevitable as the breadth of the states' general power to escheat and the corresponding potential revenue increased.¹²⁴ Originally, the test for a state's claim of sovereignty was premised on that state's contacts with the obligation.¹²⁵ However, the contacts test would ultimately prove unworkable following the practical result of two Supreme Court cases.¹²⁶

First, in *Connecticut Mutual Life Insurance Co. v. Moore*, the Court was asked to consider the validity of the New York Abandoned Property Law.¹²⁷ The statute covered unclaimed proceeds of insurance policies for New York residents issued by insurance companies incorporated in states other than New

¹²¹ McThenia & Epstein, *supra* note 35, at 1434.

¹²² *Id.*; see also *Texas*, 379 U.S. at 677; Wolfe, *supra* note 3, at 193 ("The simple situs rules . . . cannot handle any more than two states in competition for the right to escheat.")

¹²³ See Houghton et al., *supra* note 43, § V(A)(1).

¹²⁴ See McThenia & Epstein, *supra* note 35, at 1436.

¹²⁵ *Id.* at 1437.

¹²⁶ See *id.* at 1437–40 (discussing the Court's application of the contacts test in *Conn. Mut. Life Ins. Co. v. Moore*, 333 U.S. 541 (1948), and *Standard Oil Co. v. New Jersey*, 341 U.S. 428 (1951)).

¹²⁷ 333 U.S. at 542.

York.¹²⁸ The Court held that New York had sufficient contacts with the property but declined to address potential claims by other states.¹²⁹

However, three Justices dissented. Justice Frankfurter argued that the case really concerned “the conflicting claims of several States in a hotchpot of undifferentiated obligations” and therefore required proper presentation by the various interested states under the Court’s original jurisdiction.¹³⁰ Justice Jackson, with whom Justice Douglas joined, criticized the contacts test as unworkable when comparing competing states’ power to escheat since multiple states would have “sufficient contacts” with the property.¹³¹

Thirteen years later, the Court upheld the validity of the New Jersey Escheat Act in *Standard Oil Co. v. New Jersey*.¹³² The statute allowed New Jersey to escheat from a New Jersey corporation unpaid dividends whose owners’ last known addresses were located out of state.¹³³ The Court reasoned that New Jersey had power to escheat the unpaid dividends because the corporation was “amenable to process through its designated agent.”¹³⁴ Further, the Court held that the Full Faith and Credit Clause would prevent the risk of multiple liability arising from claims by other states.¹³⁵

Four Justices dissented. Justice Frankfurter, with whom Justice Jackson joined, argued that the majority’s reasoning conflicted with the holding in *Moore*, which looked to the state of the owner’s last known address.¹³⁶ Further, Justice Frankfurter was concerned that the majority holding would place the Constitution “in an unseemly light” by creating a “race of diligence.”¹³⁷ Justice Douglas, with whom Justice Black joined, listed multiple possible states that might lay claim to the unpaid dividends under the contacts test, of which only New Jersey was represented in the case.¹³⁸

¹²⁸ *Id.*

¹²⁹ *Id.* at 548–49.

¹³⁰ *See id.* at 552, 555 (Frankfurter, J., dissenting).

¹³¹ *See id.* at 558–63 (Jackson, J., dissenting).

¹³² 341 U.S. 428 (1951).

¹³³ *Id.* at 429, 437 n.8. The only “contact” that the corporation had with New Jersey was its registered office and agent, both of which were located in New Jersey. *See id.* at 437, 438.

¹³⁴ *Id.* at 438.

¹³⁵ *Id.* at 443.

¹³⁶ *Id.* at 444 (Frankfurter, J., dissenting).

¹³⁷ *Id.* Particularly, New Jersey’s Act was a true escheat statute rather than custodial, which meant that no other state would be able to lay claim to the property once the title had been transferred exclusively to New Jersey. *Id.*

¹³⁸ *Id.* at 445 (Douglas, J., dissenting).

Justice Frankfurter's concern—that the effect of the decisions in *Moore* and *Standard Oil* would create a “race of diligence”—was realized over the next decade as states broadened the reach of their unclaimed property laws and substantially shortened their dormancy periods.¹³⁹ It was not until 1961 that the Court would return to the issue and bring the race to an end in *Western Union Telegraph Co. v. Pennsylvania*.¹⁴⁰ Here, the Court held that Pennsylvania did not have the power to escheat from a New York corporation unclaimed money orders purchased in Pennsylvania by non-Pennsylvania residents, because Pennsylvania did not have the power to protect the holder corporation from potential claims by other states.¹⁴¹ The Court effectively invited any states with conflicting escheat claims to bring suit under the Court's original jurisdiction.¹⁴² Four years later, the invitation was accepted in *Texas v. New Jersey*.¹⁴³ In *Texas*, the Court would establish the current structure for resolving conflicting interstate claims.

B. Dual-Pronged Priority Structure (Texas v. New Jersey and Its Progeny)

This section lays out the current federal solution for resolving conflicting interstate claims to nearly all forms of unclaimed property. Subsection 1 traces the different options the Court considered in *Texas v. New Jersey*¹⁴⁴ to resolve interstate conflicts and outlines the dual-priority structure that it ultimately created. The dual-priority structure may be simply stated as: (1) the state in which the owner's last known address is located has the power to escheat the unclaimed property, but (2) if that state does not have a law covering the property or if there is no record of the last known address, then the state in which the holder is incorporated has the power to escheat the unclaimed property.

Subsection 2 addresses *Pennsylvania v. New York*,¹⁴⁵ in which the Court was presented with a fact situation that strained the underlying rationale of the

¹³⁹ Cary B. Hall, Note, *Escheat? Gesundheit. But for States, It's Nothing to Sneeze At: Delaware v. New York*, 113 *S.Ct.* 1550 (1993), 5 U. MIAMI BUS. L.J. 79, 88 (1994–1995); see also EPSTEIN, *supra* note 38, § 2.03 (“It was not uncommon to find abandonment periods of 14 and 20 years prior to the *Standard Oil* decision. By 1954 several states had shortened the period to seven years.”).

¹⁴⁰ 368 U.S. 71 (1961).

¹⁴¹ *Id.* at 72–73, 75.

¹⁴² See Billy F. Hicks, Comment, *Escheat in Texas: A Current Look at the Intangible Issue*, 29 *Sw. L.J.* 575, 582 (1975).

¹⁴³ 379 U.S. 674 (1965).

¹⁴⁴ *Id.*

¹⁴⁵ 407 U.S. 206 (1972).

dual-priority structure. However, the Court reaffirmed its holding in *Texas*, tilting the scales in favor of efficiency rather than equity. Subsection 3 briefly addresses the Disposition of Abandoned Money Orders and Traveler's Checks Act, in which Congress superseded *Pennsylvania* by statutorily altering the dual-priority structure for specific types of unclaimed property. Finally, subsection 4 presents *Delaware v. New York*,¹⁴⁶ the last case the Court has heard concerning the dual-priority structure. In *Delaware*, the Court refused to depart from its bright-line rule, despite further erosion of the rule's originally proffered rationale. Instead, the Court expressly deferred to Congress as the appropriate agent for resolving any specific defects in the rule.

I. *Texas v. New Jersey*

In *Texas v. New Jersey*, Texas invoked the Court's original jurisdiction and sought declaratory relief to settle which state had the right to escheat unclaimed property held by Sun Oil Company.¹⁴⁷ Four different states asserted a right to some portion of the unclaimed property, and each proposed a distinct rule to be adopted by the Court.¹⁴⁸ First, Texas proposed that the state with the most significant contacts with the debt should be entitled to escheat it.¹⁴⁹ Second, New Jersey, in which Sun Oil was incorporated, argued that the state in which the debtor is domiciled should have the right to escheat.¹⁵⁰ Third, Pennsylvania argued that the state in which the debtor's principal place of business is located should retain the exclusive right to escheat the unclaimed property.¹⁵¹ Finally, Florida argued that the right to escheat "should be accorded to the State of the creditor's last known address as shown by the debtor's books and records."¹⁵²

¹⁴⁶ 507 U.S. 490 (1993).

¹⁴⁷ *Texas*, 379 U.S. at 675. The unclaimed property in question primarily consisted of uncashed and unclaimed checks. *Id.* at 675, 677 n.4. Texas also sought a temporary injunction to enjoin the other contending states from escheating the property; however, this claim was dismissed when the states agreed to abstain from taking action until the case was resolved. *Id.* at 677 n.5.

¹⁴⁸ See *id.* at 676–77 (introducing Texas, New Jersey, Pennsylvania, and Florida as the contending states and briefly describing each proposal). Illinois had no interest in the instant property, but it sought to intervene to argue that the right to escheat "should depend on the laws of the State in which the indebtedness was created." *Id.* at 677 n.6. However, Illinois's motion to intervene was denied in an earlier proceeding. *Miscellaneous Orders*, 372 U.S. 973 (1963) (denying motion to intervene).

¹⁴⁹ *Texas*, 379 U.S. at 678.

¹⁵⁰ *Id.* at 679.

¹⁵¹ *Id.* at 680.

¹⁵² *Id.* at 680–81.

The Court then examined each of the tests in order. First, the Court rejected the contacts test as unworkable, because it would lead to such “permanent turmoil” that any benefits a state might gain from escheat would be nullified by the litigation expenses created by the uncertainty of the test.¹⁵³ Second, although the Court found the debtor’s state of incorporation test compelling in its “clarity and ease of application,” it was hesitant to adopt a test that would elevate a “minor factor” (mere incorporation) for debts incurred across the country.¹⁵⁴ Third, the Court found the principal place of business test persuasive since that state’s laws and economy substantially benefit the company responsible for the creation of the unclaimed property.¹⁵⁵ However, the Court rejected this test because it would be “strange” to convert a liability of the debtor into an asset through escheat, and additionally, the case-by-case search for a business’s principal place of business would create too much uncertainty.¹⁵⁶ Finally, the Court decided to adopt the last-known-address test because of its ability to balance fairness with clarity.¹⁵⁷ Further, the last-known-address test would ensure that escheats among the states would be distributed in proportion to “the commercial activities of their residents.”¹⁵⁸

Adopting the last-known-address test, however, left two unresolved scenarios: when the debtor’s records omit the creditor’s last known address, and when the state of last known address does not provide for escheat of the property.¹⁵⁹ Therefore, as a matter of “ease of administration and of equity,” the Court devised a dual-pronged priority structure whereby the last-known-address test takes primary priority.¹⁶⁰ However, in the event that the first-priority rule is inapplicable for either of the reasons just mentioned, the debtor’s state of incorporation test takes second priority.¹⁶¹

¹⁵³ *Id.* at 678–79.

¹⁵⁴ *Id.* at 680.

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*

¹⁵⁷ *See id.* at 680–82 (reasoning that this test incorporates fairness because “a debt is property of the creditor, not of the debtor,” and clarity because it presents “a factual issue simple and easy to resolve, and leaves no legal issue to be decided”).

¹⁵⁸ *Id.* at 681.

¹⁵⁹ *Id.* at 682. Unfortunately, it is unclear whether a state’s unclaimed property law that explicitly exempts particular forms of property would fall within the latter scenario. *See* EPSTEIN, *supra* note 38, § 2.05 (“In this instance, perhaps, the holder is not required to report because, literally, the law of the state of last known address does provide for escheat, albeit not effectively.”).

¹⁶⁰ *See Texas*, 379 U.S. at 682–83.

¹⁶¹ *See id.* However, any state escheating property under the second-priority rule would retain it until some other state proves that it has a right to escheat the property under the first-priority rule, whether by determining the residence of the creditor or by enacting legislation to cover the property in question. *Id.*

Importantly, the Court's holding was not determined "by statutory or constitutional provisions or by past decisions, nor [was] it entirely one of logic."¹⁶² Rather, the holding was premised on the belief that the dual-pronged priority structure was "the fairest, . . . easy to apply, and in the long run . . . the most generally acceptable to *all* the States."¹⁶³ Ironically, in subsequent cases, the Court's reasoning for reaffirming the dual-priority structure relied on the precedential weight of *Texas*. Although the rule is certainly easy to apply, its fairness and acceptability to all the states is doubtful in the gift card context, where a minority of states—primarily Delaware and New York, where most businesses are incorporated—benefit substantially.¹⁶⁴

2. Pennsylvania v. New York

Eleven years after *Western Union*, Pennsylvania renewed its efforts to escheat the unclaimed money orders that were the subject of that case in *Pennsylvania v. New York*.¹⁶⁵ Pennsylvania brought this original action against New York to determine which state had the right to escheat or take custody of the unclaimed money orders held by Western Union Telegraph Company.¹⁶⁶ Pennsylvania argued that in certain industries where the customary business practice is to omit from its records the address of the creditor, the state in which the transaction occurred should be permitted to escheat rather than the state in which the debtor is incorporated.¹⁶⁷ Further, to hold otherwise would entitle the state of incorporation to a windfall, and thus the *Texas* rule would not be acceptable to all the states in this particular context.¹⁶⁸ The Court recognized that there was some inconsistency between the underlying rationale in *Texas* and applying the second-priority rule here.¹⁶⁹ However, it declined to carve out an exception to the bright-line rule that would "require [the] Court to

¹⁶² *Id.* at 683.

¹⁶³ *Id.* (emphasis added).

¹⁶⁴ See *infra* Part IV.A.

¹⁶⁵ 407 U.S. 206 (1972).

¹⁶⁶ *Id.* at 207. Connecticut, California, and Indiana joined as intervening plaintiffs, and New Jersey submitted an amicus brief supporting Pennsylvania's position. *Id.* at 207 nn.1–2. Florida was an original defendant while Arizona joined as an intervening defendant. *Id.* Recall that the money orders were purchased in Pennsylvania and Western Union was incorporated in New York. See *supra* Part III.A.

¹⁶⁷ *Pennsylvania*, 407 U.S. at 213–14.

¹⁶⁸ *Id.* at 214. Pennsylvania also argued that the first-priority rule under *Texas* was merely a legal presumption that the creditor's residence was actually in the state of her last known address. *Id.* Therefore, argued Pennsylvania, a similar presumption based on the state in which the transaction occurred is equally valid and should be given greater priority than the state of incorporation. *Id.*

¹⁶⁹ *Id.*

do precisely what [it] said should be avoided” by deciding a state’s right to escheat on a case-by-case basis.¹⁷⁰

Justice Powell wrote a dissenting opinion, which Justices Blackmun and Rehnquist joined, arguing that the majority’s wooden application of the *Texas* rule “exalts the rule but derogates the reasons supporting it.”¹⁷¹ First, the rationale for relegating the debtor’s state of incorporation test to secondary priority in *Texas* was to avoid converting a debtor’s obligation into an asset and unnecessarily elevating the importance of a minor factor such as incorporation.¹⁷² However, the second-priority rule “would be impermissible as a basis for disposing of more than a small minority of the debts.”¹⁷³

Second, Justice Powell argued that the majority’s mechanical application of *Texas* failed to ensure that escheats among the states would be distributed in proportion to the commercial activities of their residents.¹⁷⁴ Finally, the majority’s holding would require the exhaustive and expensive examination of all available money order applications in search of addresses, which would defeat the utility of the *Texas* rule.¹⁷⁵

Justice Powell then argued for the application of the transactional rule as a logical deviation from *Texas*, which would preserve the “equitable foundation” of *Texas* by preventing a windfall to New York, and would require more easily obtainable information regarding the state in which the transaction occurred.¹⁷⁶ Although Justice Powell’s argument did not win the day, it was likely the impetus for Congress stepping in two years later to supersede the majority’s holding in *Pennsylvania*.

3. *Disposition of Abandoned Money Orders and Traveler’s Checks Act*

Two years later, in response to *Pennsylvania*, Congress passed the Disposition of Abandoned Money Orders and Traveler’s Checks Act, which statutorily altered the dual-priority structure as applied to money orders and

¹⁷⁰ *Id.* at 214–15. Further, the Court noted that many of the creditors’ addresses were actually available in the retained records of money order applications—as opposed to the ledger records—and the availability of these addresses would diminish any windfall to New York. *Id.* at 215.

¹⁷¹ *Id.* at 216 (Powell, J., dissenting).

¹⁷² *Id.* at 218–19.

¹⁷³ *Id.* at 219.

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Id.* at 219–20.

traveler's checks.¹⁷⁷ This Act replaced the first-priority rule from *Texas* with a place-of-purchase test, which accords the right to escheat any unclaimed funds to the state in which the money order or traveler's check was purchased as designated in the business's records.¹⁷⁸ If the records do not indicate the state of purchase, or if the state of purchase's unclaimed property laws do not provide for escheat or custodial taking of the unclaimed property, then the right to escheat is accorded to the state in which the debtor's principal place of business is located.¹⁷⁹

4. Delaware v. New York

In *Delaware v. New York*,¹⁸⁰ the Court was presented with another opportunity to refine the dual-priority structure of the *Texas* rule but declined to do so.¹⁸¹ The unclaimed property in dispute primarily consisted of unclaimed dividends, interest, and other distributions made by issuers of securities, which the issuers had transferred to intermediaries such as banks, depositories, and brokers.¹⁸² Between 1985 and 1989, New York had taken custody of \$360 million in funds held by intermediaries doing business in New York, regardless of the last known addresses of beneficial owners or the intermediaries' state of incorporation.¹⁸³ Delaware brought this original action, arguing that the securities had been wrongfully escheated by New York.¹⁸⁴

In an opinion by Justice Thomas, the Court adhered to the dual-priority rules from *Texas* and concluded that unclaimed securities distributions held by intermediaries for unidentifiable beneficial owners¹⁸⁵ escheat to the state in which the intermediary is incorporated.¹⁸⁶ First, the Court "determine[d] the

¹⁷⁷ See 12 U.S.C. §§ 2501–2503 (2006).

¹⁷⁸ *Id.* § 2503(1).

¹⁷⁹ *Id.* § 2503(2)–(3).

¹⁸⁰ 507 U.S. 490 (1993).

¹⁸¹ See *id.* at 494.

¹⁸² *Id.* at 495. The intermediaries would hold the securities in their own names, as opposed to the beneficial owners' names. *Id.* For a brief discussion of the relevant issues regarding the nature of the securities system, see generally Wolfe, *supra* note 3, at 178–88.

¹⁸³ *Delaware*, 507 U.S. at 496. The dormancy period was three years as prescribed by the New York Abandoned Property Law, whereas Delaware's unclaimed property laws prescribed a dormancy period of five to seven years. Hall, *supra* note 139, at 95. New York's law was likely an attempt by the state to avoid the issues presented by *Texas* before other states attempted to escheat the funds. *Id.* at 95–96.

¹⁸⁴ *Delaware*, 507 U.S. at 496–97.

¹⁸⁵ *Id.* at 500 ("The bulk of the abandoned distributions at issue, however, cannot be traced to any identifiable beneficial owner, much less one with a last known address.").

¹⁸⁶ *Id.* at 494.

precise debtor-creditor relationship”¹⁸⁷ by identifying the intermediaries as the appropriate debtor “because they alone . . . [were] legally obligated to deliver unclaimed securities distributions to the beneficial owners,”¹⁸⁸ and by identifying the registered shareholders as the relevant creditors because they were the parties contractually owed the unclaimed securities distributions.¹⁸⁹

Next, the Court applied the secondary rule because the identities—let alone the last known addresses—of the beneficial owners were unknown, and the Court reaffirmed that the secondary rule exclusively accords the right to escheat to the state of the debtor’s incorporation.¹⁹⁰ Strict adherence to *Texas* and *Pennsylvania* was dictated by “[p]recedent, efficiency, and equity.”¹⁹¹ Although the Court mentioned equity as part of its rationale, adherence to precedent was now more important than ensuring that the rule led to equitable results. Any inequitable gaps that the *Texas* rule failed to account for were left in the hands of Congress to remedy. The Court advocated that states may always “air their grievances before Congress” to obtain specific legislation just as was done after *Pennsylvania* with the passage of the Disposition of Abandoned Money Orders and Traveler’s Checks Act.¹⁹² Finally, the Court

¹⁸⁷ *Id.* at 499.

¹⁸⁸ *Id.* at 504–05. The Court declined to follow the Special Master’s recommendation that the relevant debtors were the issuers—an argument proposed by Texas and other intervening states—because the issuers had extinguished any and all contractual liabilities upon transfer of the distributions to the intermediaries. *See id.*

¹⁸⁹ *Id.* at 508. The Court rejected New York’s argument that the relevant creditors were other intermediary brokers who had purchased the underlying securities. *Id.*

¹⁹⁰ *Id.* at 505–07. Here, the Court declined to follow the Special Master’s sua sponte recommendation that the secondary rule should grant the right to escheat unclaimed securities to the state in which the debtor’s principal executive offices are located. *Id.* at 505–06. The Special Master reasoned that strict adherence to the state of incorporation standard would inequitably grant a windfall to Delaware, whereas a principal executive office standard would more evenly distribute the unclaimed funds. *Id.* at 507. However, since the Court identified the relevant debtors as the intermediaries, whose principal executive offices were primarily located in New York, the proposed standard would merely shift the windfall to another state and would needlessly complicate the desirable simplicity and efficiency of the secondary rule under *Texas*. *Id.* at 506–07.

The Court also rejected New York’s argument that the primary rule should be augmented by utilizing statistical sampling instead of the debtor’s records to locate creditors’ last known addresses. *Id.* at 508–09. The Court quickly dismissed this argument, which was “practically identical” to Pennsylvania’s proposed place-of-purchase standard in *Pennsylvania*. *Id.* (citing *Pennsylvania v. New York*, 407 U.S. 206, 214 (1972)).

¹⁹¹ *Id.* at 507. Although the *Texas* Court acknowledged that the interstate dispute issue is not controlled by past decisions, *Texas v. New Jersey*, 379 U.S. 674, 683 (1965), the *Delaware* Court reasoned that adherence to precedent was necessary to preserve efficiency and equity, 507 U.S. at 510.

¹⁹² *Delaware*, 507 U.S. at 510 (citing 12 U.S.C. §§ 2501–2503 (2006)). In fact, the majority of states decided to air their grievances within less than a year, when the Equitable Escheatment Act of 1993 was introduced into Congress. *See* H.R. 2443, 103d Cong. (1993); S. 1715, 103d Cong. (1993). This Bill, if passed, would have altered the secondary rule and introduced a third-priority rule regarding unclaimed distributions paid on securities. *See* H.R. 2443, 103d Cong. (1993); S. 1715, 103d Cong. (1993).

noted that the *Texas* rule was federal common law, which would preempt any state laws that “prescribe a different priority” structure.¹⁹³ This is particularly significant because it means that states lack the power to exempt gift cards, or any other forms of unclaimed property, if the *Texas* rule would entitle another state to claim that property.¹⁹⁴

C. Summary

The past sixty years of Supreme Court jurisprudence reflect a departure from determining the scope of unclaimed property laws to outlining which states have the exclusive right to escheat unclaimed property. Ultimately, the Court devised a rule that was—in theory—both efficient in its administration and equitable to all the states. However, as particular situations arose that yielded inequitable results under the *Texas* rule, the Court continuously upheld its rule by emphasizing efficiency over equity. The Court has effectively washed its hands of any case-specific inadequacies by deferring to Congress as the appropriate outlet for remedying such inequitable results.

IV. THE NEED FOR CONGRESSIONAL ACTION: WHY THE DUAL-PRIORITY STRUCTURE IS UNSUITABLE FOR GIFT CARDS

This Part argues that the *Texas* dual-priority structure is wholly inadequate in the context of gift cards. Section A argues that the *Texas* rule necessarily collapses into a single rule for gift cards and inequitably benefits a minority of states, particularly Delaware and New York. Additionally, it concludes that the Supreme Court is unlikely to revisit interstate conflicts of escheat laws, despite gift cards presenting the ideal context for carving out an exception to the Court’s bright-line rule. Sections B and C analyze the other two possible outlets for reform—the states and Congress, respectively. Section B argues that although it would seem states are in the best position to resolve an area traditionally relegated to their sovereignty, the *Texas* rule preempts any state attempts to create a uniform and equitable rule. Section C concludes that Congress is the only viable avenue for providing an equitable solution.

¹⁹³ See *Delaware*, 507 U.S. at 500 (“[N]o State may supersede [the *Texas* rule] by purporting to prescribe a different priority under state law.”).

¹⁹⁴ See *infra* Part IV.B.

A. *And Then There Was One: The Collapse of the Dual-Priority Rule*

Under the *Texas* rule, the primary rule of last known address will never be satisfied in the gift card context. Even in the unlikely situation that a business retains records of a gift card purchaser's last known address, the purchaser is not the owner.¹⁹⁵ Instead, the owner is the subsequent recipient of the gift card.¹⁹⁶

Consequently, the dual-priority structure collapses into a single rule for gift cards, so that the state of the holder's incorporation will always have the power to escheat the breakage as long as it has legislation covering gift cards.¹⁹⁷ This means that Delaware, which is the state of incorporation for more than half of publicly traded companies,¹⁹⁸ is the primary recipient of unclaimed gift card revenue. In fact, unclaimed property accounts for Delaware's third largest source of revenue.¹⁹⁹ Therefore, a strict application of the dual-priority structure ensures a windfall to Delaware, which contradicts the rationale for a rule that is "most generally acceptable to all the States."²⁰⁰

In *Pennsylvania v. New York*, Justice Powell argued in his dissent that the *Texas* rule should not be woodenly applied to situations that would elevate the incidental factor of incorporation to an impermissible degree,²⁰¹ particularly when its rigid application would arbitrarily and inequitably bestow a single state with a "windfall."²⁰² The majority dismissed Justice Powell's windfall argument because the money order applications included records of the owners' last known addresses, so the dual-priority rule would not necessarily collapse into the secondary rule of incorporation.²⁰³ However, Justice Powell's argument is far more convincing in the gift card context where the last known addresses of gift card owners are necessarily unavailable.²⁰⁴ In this case, it is

¹⁹⁵ See NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 15–16 (“[M]ost gift cards are given to another person . . .”).

¹⁹⁶ *Id.*

¹⁹⁷ See *id.* at 16.

¹⁹⁸ Lucian Arye Bebchuk & Assaf Hamdani, *Vigorous Race or Leisurely Walk: Reconsidering the Competition over Corporate Charters*, 112 YALE L.J. 553, 553–54 (2002).

¹⁹⁹ See *Minutes of the Delaware Economic & Financial Advisory Council*, DEL. DEP'T OF FIN., 4 tbl. (June 15, 2009), http://finance.delaware.gov/defac/min_0609.pdf.

²⁰⁰ *Texas v. New Jersey*, 379 U.S. 674, 683 (1965).

²⁰¹ *Pennsylvania v. New York*, 407 U.S. 206, 218–19 (1972) (Powell, J., dissenting).

²⁰² See *id.* at 220.

²⁰³ See *supra* note 170 and accompanying text.

²⁰⁴ As discussed above in Part II.A, states *could* require businesses to obtain owners' personal information; however, this would not present an ideal solution due to consumer privacy concerns.

difficult to deny that a minority of states will be entitled to the majority of unclaimed gift card revenue.

Unfortunately, the Supreme Court has made it clear that the efficiency of a bright-line rule is, in its estimation, preferable to equitable results. Therefore, the Court is not the appropriate branch for tailoring the dual-priority structure to gift cards.

B. Preemption of States' Attempts to Carve in Additional Priority Rules

This section addresses attempts by individual states to carve in a tertiary rule based on the state in which the transaction occurred. This third-priority rule would take effect when neither the primary nor the secondary rule identifies a particular state. However, it is unclear whether the *Texas* rule, which is federal common law, would preempt states from enforcing additional rules of priority. This uncertainty amplifies the risks of compliance for businesses that have incorporated in states that exempt gift cards from their unclaimed property laws. On the one hand, if the third-priority rule is enforceable, then such businesses would be required to report gift card breakage to states in which the gift card was purchased. On the other hand, if the third-priority rule is preempted, then the business may retain the breakage. This section concludes that because the dual-priority structure is federal common law, any state's attempt to create additional priority rules is likely preempted. Therefore, the only viable solution that remains depends on congressional action.

1. The 1981 and 1995 Uniform Acts

Both the 1981 Act and the 1995 Act incorporate the priority rules as declared in *Texas*.²⁰⁵ The 1995 Act also incorporates the Disposition of Abandoned Money Orders and Traveler's Checks Act.²⁰⁶ However, the Acts include an additional provision, which creates a third-priority rule enabling the state in which the formative transaction occurred to escheat the intangible property when the primary and secondary rules would not apply.²⁰⁷ In other words, the proposed tertiary rule unearths the contacts test that was rejected in

²⁰⁵ See 1981 UNIF. ACT, *supra* note 75, § 3(1), (3), 8C U.L.A. at 189; 1995 UNIF. ACT, *supra* note 12, § 4(1), (3), 8C U.L.A. at 111, 112.

²⁰⁶ See 1995 UNIF. ACT, *supra* note 12, § 4(7), 8C U.L.A. at 112.

²⁰⁷ *Id.* § 4(6), 8C U.L.A. at 112; 1981 UNIF. ACT, *supra* note 75, § 3(6), 8C U.L.A. at 189. Of course, a state asserting custody under this rule would retain the unclaimed property, subject to any state with a greater claim under the primary or secondary rules.

Texas. The rationale for including this provision is that when neither of the *Texas* priority claims apply, but another “[s]tate has a genuine and important contact with the property,” that state should be entitled to escheat the property to avoid a windfall to the private debtor.²⁰⁸

However, the legitimacy of creating rules of priority beyond the dual-priority structure construed in *Texas* remains questionable at best, particularly given the holding in *Texas* was intended to settle the issue of conflicting state claims “once and for all by a clear rule.”²⁰⁹ Further, many states have expressly omitted or exempted particular forms of intangible property from their unclaimed property laws²¹⁰ to attract businesses to incorporate in their state. Allowing other states to claim these forms of property would nullify the intent of such exemptions.

Unfortunately, the Supreme Court has not addressed whether the *Texas* dual-priority structure preempts the construction of additional, but not necessarily conflicting, priority rules.²¹¹

2. *A Split in the Caselaw Increases the Risk of Compliance*

Although the Supreme Court has yet to address whether the dual-priority structure preempts state laws from devising additional priority rules, the lower courts have confronted the issue to a limited degree with varying results. The risks of compliance for businesses implementing gift cards are already too great,²¹² and the questionable enforceability of a third-priority rule will only increase these risks.

The argument supporting the validity of a tertiary rule is that the dual-priority structure devised in *Texas* relates only to disputes between states, and

²⁰⁸ 1995 UNIF. ACT, *supra* note 12, § 4 cmt., 8C U.L.A. at 113; *see also* NETWORK BRANDED PREPAID CARD ASS’N, *supra* note 56, at 3 (noting that an objective of the Uniform Acts was the prevention of an unjust windfall to property holders). The comment to the 1995 Act expressly indicates that the third-priority rule applies to gift certificates when there is no last known address and when the state of incorporation does not have an abandoned property law covering gift certificates. 1995 UNIF. ACT, *supra* note 12, § 4 cmt., 8C U.L.A. at 114.

²⁰⁹ *Texas v. New Jersey*, 379 U.S. 674, 678 (1965).

²¹⁰ *See, e.g.*, ARIZ. REV. STAT. ANN. § 44-301(15) (2010); ARK. CODE ANN. § 18-28-201(13)(B)(i) (2009); CONN. GEN. STAT. § 3-73a(e) (2008); IND. CODE § 32-34-1-1(f) (2009); MD. CODE ANN., COM. LAW § 17-101(m) (LexisNexis 2010); *cf.* *Delaware v. New York*, 507 U.S. 490, 507 (1993) (“When the creditor’s State cannot assert its predominant interest, we detect no inequity in rewarding a State whose laws prove more attractive to firms that wish to incorporate.”).

²¹¹ *Houghton et al.*, *supra* note 43, § V(B)(1).

²¹² *See supra* Part II.C.

therefore, *Texas* does not prohibit a state from taking custody of property based on a tertiary rule as long as that state is capable of protecting the holder from multiple liability.²¹³ Conversely, other courts have supported the conclusion that the dual-priority structure preempts any state laws that would attempt to expand the available rules of priority.²¹⁴ In *American Petrofina Co. v. Nance*,²¹⁵ the U.S. District Court for the Western District of Oklahoma held that federal common law, developed to resolve disputes between states, may be applied to suits between private litigants.²¹⁶ More recently, in 2010, the U.S. District Court for New Jersey granted a preliminary injunction enjoining New Jersey from enforcing its place-of-purchase presumption because there was a reasonable probability that federal common law preempts the statutory attempt to create a new rule of priority.²¹⁷

²¹³ See, e.g., *State v. Chubb Corp.*, 570 A.2d 1313, 1315–16 (N.J. Super. Ct. Ch. Div. 1989) (“Nothing in *Texas v. New Jersey* . . . prohibits a state from claiming custodial escheat of property based on the locale of the transaction or the place of business of the holder being in that state.”); *TXO Prod. Corp. v. Okla. Corp. Comm’n*, 829 P.2d 964, 971 (Okla. 1992) (“In *Texas* the Court was not confronted with, nor did it decide, the rights to custody of abandoned property *as between a private holder and a State*. . . . Nothing in *Texas* prohibits a state from claiming temporary custody of unclaimed property until some other state comes forward with proof that it has a superior right to it.”); *O’Connor v. Sperry & Hutchinson Co.*, 379 A.2d 1378, 1381 (Pa. Commw. Ct. 1977), *aff’d*, 412 A.2d 539 (Pa. 1980).

²¹⁴ See *Am. Petrofina Co. v. Nance*, 697 F. Supp. 1183, 1187–88 (W.D. Okla. 1986) (holding that state laws are preempted to the extent they conflict with federal common law, particularly when devised for the purpose of national uniformity), *aff’d*, 859 F.2d 840 (10th Cir. 1988).

²¹⁵ *Id.*

²¹⁶ *Id.* at 1187 (“The rules of federal common law developed in resolving disputes between states have been applied not only to suits between states but to suits between private litigants as well.”).

²¹⁷ *Am. Express Travel Related Servs. Co. v. Sidamon-Eristoff*, No. 4890 (FLW), 2010 U.S. Dist. LEXIS 120153 (D.N.J. Nov. 13, 2010), *clarified sub nom.* *N.J. Retail Merchs. Ass’n v. Sidamon-Eristoff*, No. 10-5059 (FLW), 2011 U.S. Dist. LEXIS 3911 (D.N.J. Jan. 14, 2011). The statute in question was N.J. STAT. ANN. § 46:30B-42.1(c) (West 2010), which provided that if the issuer did not have the purchaser’s or owner’s name and address, then that address would be deemed to be the same address as the place where the card was purchased. *Am. Express*, 2010 U.S. Dist. LEXIS 120153, at *107–08. The State argued that “it may create a ‘third priority rule’ under which it temporarily holds the property until the creditor’s address becomes apparent and the creditor’s state asserts its superior right to escheat.” *Id.* at *128.

The court acknowledged the cases cited above in note 213, but went on to argue that their underlying rationale could “not withstand more careful examination,” *id.* at *129, and concluded that “there is no room for a third priority position[;] . . . [i]f the secondary-rule state does not escheat, the buck stops there,” *id.* at *133. The court’s preemption analysis relied on the language in *Delaware v. New York* that “no State may supersede [*Texas* and *Pennsylvania*] by purporting to prescribe a different priority under state law.” *Id.* at *134 (quoting *Delaware v. New York*, 507 U.S. 490, 500 (1993)) (internal quotation marks omitted). Further, the Supreme Court had considered multiple possible schemes, of which it selected only one, which implied that the Court intended the dual-priority structure to remain precisely that. *Id.* at *135. To allow states to create any number of new rules of priority would defeat the ease of administration for which the Court selected its bright-line rule. *Id.* at *136.

Given the Supreme Court's repeated strict adherence to the dual-priority structure set out in *Texas* because of its ease in application,²¹⁸ and the Court's rejection of a contacts test that would create "permanent turmoil" on an issue in need of national uniformity,²¹⁹ the reasoning of the *Nance* and *American Express* courts is far more compelling²²⁰ than the desire to prevent holders from receiving a windfall under any and all circumstances. Both potential holders and state legislatures, which have enacted express exemptions in their unclaimed property laws, have relied on the *Texas* rule over the past four decades. Muddying the waters with potentially unlimited additional priority rules among the states would re-create the very problem that the *Texas* Court set out to resolve.

Businesses implementing gift cards are subjected to further uncertainty by attempts of states to carve in a tertiary transactional rule. For example, many businesses create a subsidiary entity specifically to manage gift card programs and to act as an intermediary holder, while the parent business acts as the agent of the subsidiary in the sale of gift cards.²²¹ The subsidiary incorporates in a state that has exempted gift cards from its escheat laws.²²² However, a state that has adopted the 1995 Act would purportedly enable that state to assert a claim against the special-purpose subsidiary despite the state of incorporation's explicit exemption.²²³ The legitimacy of state attempts to create additional rules of priority remains unclear²²⁴ and only heightens the uncertainty and corresponding risk of noncompliance for businesses employing gift cards.²²⁵ Consequently, the only outlet for creating or refining the rules of priority will depend on congressional action.

C. Congressional Action Is Appropriate

Sections A and B argued that neither the Supreme Court nor the states are well equipped to resolve issues of gift cards under the current system of

²¹⁸ See *Delaware*, 507 U.S. at 506, 507; *Pennsylvania v. New York*, 407 U.S. 206, 211, 215 (1972); *Texas v. New Jersey*, 379 U.S. 674, 683 (1965).

²¹⁹ *Texas*, 379 U.S. at 678.

²²⁰ Perhaps unsurprisingly, the cases on point have a clear dividing line: state courts have dismissed preemption claims whereas the cases striking down states' attempts have been adjudicated in federal district courts.

²²¹ John A. Biek, *Unredeemed Gift Cards and Stored Value Cards Present Unclaimed Property and Income Tax Issues*, J. PASSTHROUGH ENTITIES, Sept.–Oct. 2008, at 13, 16.

²²² *Id.*

²²³ Houghton et al., *supra* note 43, § V(B).

²²⁴ See *supra* Part IV.B.

²²⁵ See *supra* Part II.C.

unclaimed property laws. The current system provides a windfall to a minority of states and creates greater uncertainty that entails increased risks of compliance. This section argues that Congress has the power to enact legislation specifically addressing gift cards, not only in the context of interstate disputes but also regarding intrastate substantive provisions of unclaimed property laws.

Congress clearly has the power to enact legislation regarding interstate conflicts. The Supreme Court expressly invited congressional action in *Delaware v. New York*.²²⁶ Further, Congress has already enacted specific legislation regarding interstate disputes of money orders and traveler's checks when it passed the Disposition of Abandoned Money Orders and Traveler's Checks Act.²²⁷

Although unclaimed property laws have traditionally been classified as a state power, Congress has the power under the Commerce Clause²²⁸ to enact legislation that specifically addresses substantive provisions regarding the escheat of gift cards. For example, Congress has expressly preempted state escheat laws regarding veterans' property²²⁹ as well as income tax refunds.²³⁰ Congress's recent enactment of the Credit CARD Act of 2009 specifically addresses consumer protection laws regarding gift cards.²³¹ Consequently, Congress has the power to statutorily alter the priority structure as applied to gift cards. More significantly, it has the power to enact a national exemption of gift cards from state escheat laws.

V. WHY CONGRESS SHOULD CREATE A BLANKET EXEMPTION FOR GIFT CARDS

This Part argues that congressional exemption of gift cards from escheat laws is the best practical solution for resolving the intrastate and interstate problems that are applicable in the gift card context. Section A argues that a

²²⁶ *Delaware v. New York*, 507 U.S. 490, 510 (1993).

²²⁷ *See supra* Part III.B.3.

²²⁸ *See Wolfe, supra* note 3, at 218.

²²⁹ *See United States v. Oregon*, 366 U.S. 643 (1961) (recognizing the validity of 38 U.S.C. § 17 (1952) (current version at 38 U.S.C. § 8520 (2006)), a federal escheat statute regarding veterans' property).

²³⁰ *See* 26 U.S.C. § 6408 (2006).

²³¹ *See* Credit CARD Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734 (codified as amended in scattered sections of 15 U.S.C.). Unfortunately, the Credit CARD Act of 2009 is generally silent on the issue of escheat, *see* 15 U.S.C. § 1693q (Supp. III 2009), and the regulations defer to the Federal Reserve Board to determine on a case-by-case basis whether a state statute is preempted by the Act, *see* 12 C.F.R. § 205.12(b) (2010).

national exemption of gift cards from escheat laws properly resolves the intrastate conflicts between holders and a given state, and conforms to the general trend of states to exempt gift cards from their escheat laws. Section B argues that this exemption will remove gift cards from a dual-priority scheme that is not equipped to encompass them. Finally, section C argues that a gift card exemption will incentivize further innovation in a rapidly developing industry and increase national and global competition.

A. *Resolution of Intrastate Conflicts*

The traditional justifications for escheat do not apply to gift cards and, therefore, exempting gift cards appropriately removes them from the subject matter of laws that were never intended to include them. States lack the ability to reunite owners with the unclaimed breakage because owners' identities are necessarily anonymous.²³² If anything, businesses are better positioned to reunite owners with their unclaimed property through optional registration programs that enable the owner to reclaim the funds in the event of loss, instead of through inconvenient state escheat procedures.²³³ Allowing businesses to retain the breakage enables them to pass on the savings to a closely tailored subgroup that is more likely to encompass the purchasers and owners of gift cards.²³⁴

Exempting gift cards ensures that state escheat laws do not violate the derivative rights doctrine by granting a greater right in the state than the owners ever had.²³⁵ A national exemption would eliminate the need for courts to resolve whether the limited right to merchandise is a condition that would be unreasonable for a state to satisfy.²³⁶

Most significantly, exempting gift cards from escheat laws substantially reduces the needless risks of compliance that businesses are subjected to in navigating through a multiplicity of states with variant, ambiguous, and antiquated legislation.²³⁷ The market for gift cards has expanded to a national level that requires uniformity.²³⁸ Even if many states were to independently

²³² See *supra* Part II.A.

²³³ See *supra* Part II.A.

²³⁴ See *supra* Part II.A.

²³⁵ See *supra* Part II.B.

²³⁶ See *supra* Part II.B.

²³⁷ See *supra* Part II.C.

²³⁸ See *supra* Part II.C.

update their legislation, the risk of nonuniformity would still remain.²³⁹ A congressional exemption properly recognizes the unique characteristics of gift cards.

B. Resolution of Interstate Conflicts

The Supreme Court's dual-priority structure falls incredibly short in accounting for gift cards because the structure necessarily collapses into a single rule based on the incidental factor of a business's state of incorporation.²⁴⁰ This entails that a minority of states receive the majority of unclaimed gift card revenue.²⁴¹ This result is completely at odds with notions of equity among the states.²⁴²

Although a blanket exemption might first appear to offer equality among the states by merely removing the benefit altogether, it is important to note three things. First, the majority of states presently receives little to no benefit from the state of incorporation rule. Short of obtaining a congressionally sanctioned compact, these states lack the power to alter the dual-priority structure.²⁴³ In fact, even if every state except for Delaware exempted gift cards from their escheat laws, the distribution of unclaimed gift card revenue would not substantially differ from the current system.

Second, a national exemption would actually benefit many states that receive little benefit under the present rule. Any breakage that a business retains as revenue would be subject to state taxes in any states with which that business has a sufficient connection.

Finally, more than half the states presently exempt gift cards to some extent for many of the reasons already mentioned. The dual-priority structure undermines the intent of these states by enabling other states to escheat gift cards that would otherwise be exempt. This concern is even greater if the third-priority rule is not preempted by *Texas v. New Jersey*. In this case, even businesses incorporated in states that exempt gift cards are at risk of other states claiming a right to escheat.²⁴⁴ A blanket exemption avoids this conflict

²³⁹ See *supra* Part II.C.

²⁴⁰ See *supra* Part IV.A.

²⁴¹ See *supra* Part IV.A.

²⁴² See *supra* Part IV.A.

²⁴³ See *supra* Part IV.B.

²⁴⁴ See *supra* Part IV.B.

and conforms to the general trend of the states to escheat gift cards from their unclaimed property laws.

C. Incentives for Innovation

Currently, the United States is the leader in the development of prepaid cards.²⁴⁵ However, expansive unclaimed property legislation—particularly when ambiguous and varying substantially from one state to the next—will lead to two consequences. First, as the United States expands prepaid and gift cards to an international market, it will face increased competition from other countries, in which retailers do not lose gift card breakage.²⁴⁶ However, if Congress passes a national exemption of gift cards, American businesses will be able to compete globally on an even playing field. This exemption would incentivize companies to continue to improve current systems.

Second, when otherwise anticipated profits are captured by states, those costs are passed on to the consumers.²⁴⁷ Creating and managing a system of gift cards includes transactional costs for the business. These costs are likely to be passed on to consumers in some fashion, whether by increasing the retail price of goods or including fees on gift cards. However, a blanket exemption would enable a business to account for these transactional costs through the retained breakage and would likely have the opposite effect of reducing the retail price of goods.

The market for gift cards has risen to a national level and requires uniform legislation. States have become more aggressive in their search for nontax revenue to the point that they have enacted legislation to grab unclaimed funds from businesses incorporated in states with business-friendly unclaimed property laws.²⁴⁸ A federal exemption to the escheat of gift cards would provide businesses with incentives to further develop gift card technology and would provide consumers with lower costs and increased convenience.

CONCLUSION

Gift cards present unique issues for current unclaimed property laws, such as the inability of states to reunite owners with their property, special

²⁴⁵ NETWORK BRANDED PREPAID CARD ASS'N, *supra* note 56, at 18.

²⁴⁶ *Id.* at 19.

²⁴⁷ *Id.*

²⁴⁸ *See supra* Part IV.B.

considerations under the derivative rights doctrine, and impractical uncertainties of how to apply current laws that were not designed to anticipate issues particular to gift cards. These reasons tend to justify the recent trend by many states to exempt gift cards from their unclaimed property laws.

However, as long as some states continue to escheat gift card breakage, these problems will continue to manifest themselves, even when the states in which the cards are purchased, sold, and used explicitly exempt gift cards from their escheat laws. This result is primarily due to the Supreme Court's strict adherence to the bright-line dual-priority structure, which enables a minority of states, in which a majority of businesses are incorporated, to capture gift card breakage.

Congress should accept the invitation of the Supreme Court to enact specific legislation regarding issues like those presented by the nuances of gift cards. Federal legislation should exempt gift cards from unclaimed property laws because gift cards are not an appropriate subject matter of escheat and because gift cards do not fit in the priority scheme of escheat among the states. A blanket congressional exemption of gift cards resolves these difficulties and increases the incentives for development in a rapidly growing national industry.

SEAN M. DIAMOND*

* Executive Managing Editor, *Emory Law Journal*; J.D. Candidate, Emory University School of Law (2011); B.A., Kenyon College (2004). I wish to thank my colleagues on the *Emory Law Journal*, particularly David Hudson for his timely insight, and Ross Andre, Jena Sold, and Rachel Mondl for their invaluable comments and revisions. I could not have written this without the constant love, support, and patience of Amanda Bissell.