



AUDITS, INTERNAL CONTROL, and RECORD KEEPING

August 2005

All businesses operating in the State of North Dakota must annually report unclaimed property to the State Land Department by November 1st. Adequate internal controls and complete records help safeguard the unclaimed property. Good accounting procedures and controls provide documentation in case of an audit.

AUDITING

The Unclaimed Property Division examines the records of financial institutions, insurance companies, and other businesses throughout the state for compliance with the Uniform Unclaimed Property Act. An audit can consider the last seven reporting years plus the current year and may be assigned for the following reasons:

- Size and type of business.
- Reporting history (or the lack thereof).
- Industry compliance emphasis (such as banks or insurers).
- Tips relating to unclaimed property.

A business that fails to file an annual unclaimed property report significantly increases the likelihood of an audit. The Unclaimed Property Administrator routinely audits companies that do not file annual unclaimed property reports or those that consistently file negative reports certifying they have no unclaimed property.

Since an audit situation can result in an assessment of audit costs and/or interest charges on past due unreported property, we typically do not call an audit without first attempting to contact the business to come into compliance on their own.

Once an audit is assigned to an auditor, the following occurs:

- The organization is notified by letter with a follow up phone call that they have been selected for examination.
- The auditor requests an opening conference with the organization. On site work will begin on the date of the opening conference.

Each audit consists of the following stages:

- Opening conference
- On-site work
- Exit conference
- Closing conference

Opening Conference

The auditor contacts the business to arrange an opening conference with the company's authorized representative. The meeting is held at the organization's place of business. The company is encouraged to invite all interested parties to this meeting.

During the conference:

- The participants may ask questions.
- The auditor learns about the organizational structure and location of records.
- The organization's liaison is appointed.
- The records request list is discussed.

On-Site Work

The examination is conducted at the location of the organization's business records. The actual amount of time working on-site will vary depending on the size and type of organization, compliance with pre-audit requests, and availability of records. On-site work for an average audit can take approximately four days to complete.

Based on the auditor's initial review, audit work may be limited in scope to selected property types or reporting periods.

Exit Conference

When the on-site work is completed, the auditor will present preliminary findings to the business at an exit conference.

The auditor will generally allow the organization approximately 30 days to:

- research the findings,
- complete due diligence and reissue checks, and
- develop adjustments to the preliminary findings.

Closing Conference

The auditor will schedule a closing conference, usually by phone, to review the organization's refunds and proposed adjustments to the findings. If there is agreement, the auditor will issue an audit report listing results. The Unclaimed Property Administrator will issue a demand letter to the organization requesting a consolidated unclaimed property report and remittance for the audit period. If agreement cannot be reached, the organization can begin appeal procedures which are discussed later in this document.

COMMON ERRORS FOUND IN AUDIT

Below are some common problems found in audits:

- Small credit balance write-offs were not reported as required.
- Property was not aged for abandonment correctly.
- Some disbursement accounts were not reviewed for unclaimed checks.
- Inactivity-based fees were taken incorrectly and were disallowed.
- Stock and dividends held at the transfer agent were not reported.
- Reportable property was not properly transferred to new system in computer conversion.

CHARGES, INTEREST, AND PENALTIES

Unreported property may be charged late payment interest from the date the property was due until paid. The interest rate is set by statute, 12% per annum, in accordance with NDCC 54-44-07.

If we have evidence that a business is not acting in good faith, the following charges, interest, and penalties may be considered:

- A fee of \$100 per auditor, per day may be charged for each day of on-site work, but charges may not exceed the value of the property found to be reportable and deliverable.
- A civil penalty of \$100 a day may be assessed for each day a report is willfully withheld or other duties are not performed. Penalty charges may not exceed the value of the property found to be reportable and deliverable.

A person who willfully fails to pay or deliver property as required shall pay a civil penalty equal to 25% of the value of the property that should have been paid or delivered. If a person, after written demand refuses to pay or deliver property is guilty of a class B misdemeanor.

The Unclaimed Property Division welcomes cooperative compliance. We see our ability to audit and to assess audit costs and interest charges, not as our first course of action, but rather as a last resort.

APPEAL PROCEDURES

If we cannot reach agreement on the audit results or application of law, the auditor will issue a draft report and a formal demand letter for the property in question will be issued by the Unclaimed Property Administrator. A business owner who is aggrieved by an audit that requests payment of money or a civil penalty is entitled to a hearing before the Board of University and School Lands. A hearing request must be made within 30 days of the demand letter issued by the Administrator. The Administrator's request must contain notice of the right to a hearing.

The Board's decision is the final order of the agency and is appealable to the District Court. Any amount of money requested by the Administrator which may increase over time is totaled at the time of filing an appeal, retroactive to the date of the request.

INTERNAL CONTROL

Abandoned property presents a strong temptation for embezzlement and fraud. Because the lost owner is unlikely to monitor the funds, adequate internal controls are needed to safeguard the unclaimed property prior to reporting.

Organizations sometimes shortcut the needed internal controls because:

- The unclaimed property amounts are considered immaterial.
- They believe their normal internal controls are adequate.

When the owner is missing, normal controls may not be enough to prevent embezzlement and fraud.

Here are some ways to avoid possible embezzlement or fraud:

- Separate stale-dated checks and aged customer credit to an unclaimed property liability account.
- Create procedures to provide management control over transactions entering and exiting the unclaimed property liability account(s).
- Have a second person independently reconcile the account on a regular basis and test the validity of refunds from the account if necessary.
- Have two employees approve refunds or other transactions from unclaimed accounts.
- Separate the duties of tracking and reporting unclaimed property from issuing refunds.

You can ask your accountant or internal auditor to help design your internal control plan. They may want to periodically perform an internal control review. This may include a verification of the amounts held in your

unclaimed property liability account back to the source records, and traced forward to refund approvals and the unclaimed property reports.

Each organization should assess its own risk and resources, and plan accordingly. Companies who suffer embezzlement often underestimated the risk or shortcut adequate internal controls in the name of efficiency.

RECORD RETENTION

ND Century Code, section 47-30.1-17 requires all organizations to maintain a record of the name and last known address of the owner for ten years after the property becomes reportable.

If you sell traveler's checks, money orders, or other similar written instruments, you must maintain a record of those items for three years after the date the property becomes reportable.

Your records must show:

- state where the instrument was issued,
- last known address, if available, and
- the issue date.

Insurance companies should keep the following information whenever there is a change of beneficiary under a life policy, an endowment policy, or an annuity contract:

- beneficiary name,
- address, and
- relationship to the insured.

As an audit trail and internal control measure, consider keeping documentation supporting any refund or adjustment to your unclaimed property liability account for ten years.

NEED HELP?

ON-SITE ASSISTANCE IS AVAILABLE

For holders located in North Dakota, representatives are available to visit your organization to answer your unclaimed property reporting questions. There is no charge for an unclaimed property consultation. A consultation visit will help you avoid mistakes and will reduce your likelihood of being selected for an audit.

UNCLAIMED PROPERTY CONTACT INFORMATION

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