

HOUSE BILL REPORT

HB 2564

As Reported by House Committee On:
Financial Institutions & Insurance

Title: An act relating to escrow agents.

Brief Description: Regarding escrow agents.

Sponsors: Representatives Nelson, Chase and Kirby; by request of Department of Financial Institutions.

Brief History:

Committee Activity:

Financial Institutions & Insurance: 1/14/10, 1/19/10 [DPS].

Brief Summary of Substitute Bill

- Makes numerous changes to the licensing and bonding requirements, prohibited activities, and enforcement provisions of the escrow agent licensing laws.

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Kirby, Chair; Kelley, Vice Chair; Bailey, Ranking Minority Member; Hurst, McCoy, Nelson, Rodne, Santos and Simpson.

Minority Report: Do not pass. Signed by 2 members: Representatives Parker, Assistant Ranking Minority Member; Roach.

Staff: Alison Hellberg (786-7152).

Background:

Licensing Requirements.

Escrow agents must be licensed by the Department of Financial Institutions (DFI).

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Among others, a person licensed to practice law in Washington is exempt from the licensing requirements while engaged in the performance of his or her professional duties. When submitting an application for an escrow agent license, an applicant must include fingerprints for all officers, directors, owners, partners, and controlling persons.

Applicants for an escrow office license must successfully pass an examination. The examination covers:

- the principles of real estate conveyancing and the general purposes and legal effects of deeds, mortgages, deeds of trust, contracts of sale, exchanges, rental and optional agreements, leases, earnest money agreements, personal property transfers, and encumbrances;
- the obligations between principal and agent;
- the meaning and nature of encumbrances upon real property;
- the principles and practice of trust accounting; and
- the Escrow Agent Registration Act and other applicable law.

The examination is developed by the DFI with the advice of the Escrow Commission, and must be given at least annually.

Bonding.

An applicant for an escrow agent license must provide evidence of the following as evidence of financial responsibility:

- a fidelity bond providing coverage in the amount of \$200,000 with a deductible no greater than \$10,000;
- an errors and omissions policy providing coverage in the amount of \$50,000 or, alternatively cash or securities in the principal amount of \$50,000 deposited in an approved depository; and
- a surety bond in the amount of \$10,000.

A "fidelity bond" is a primary commercial blanket bond or its equivalent. The bond must provide fidelity coverage for any fraudulent or dishonest acts committed by employees or officers, acting alone or in collusion with others. The bond is for the sole benefit of the escrow agent and under no circumstances is the bonding company liable under the bond to any other party.

Prohibited Activities.

Escrow agents are prohibited from engaging in certain activities, for example, engaging in any unfair or deceptive practice toward any person and making any false entry, or omitting to make any material entry, in its books or accounts.

Enforcement.

The DFI may deny, suspend, decline to renew, or revoke the license of any escrow agent or escrow officer for various prohibited activities. In addition to or in lieu of a license suspension, revocation, or denial, the DFI may assess a fine of up to \$100 per day for each day's violation and may remove and/or prohibit from participation in the conduct of the affairs of any licensed escrow agent, any officer, controlling person, director, employee, or licensed escrow officer.

Summary of Substitute Bill:

Licensing Requirements.

The exemption for those licensed to practice law is clarified. The exemption only applies when no separate compensation or gain is received for escrow services, and the service is provided by the same legal entity as the law practice. An attorney who is principally engaged as an escrow agent, or holding himself or herself out to perform escrow services, is required to be licensed.

Applicants must undergo a fingerprint-based background check. The DFI may also request criminal history record information, including nonconviction data. The DFI may disseminate nonconviction data obtained only to criminal justice agencies and the applicant must pay the cost of fingerprinting and processing the fingerprints.

The license renewal procedures are modified. If a license is not renewed on or before the renewal date, the license is expired and any activity conducted is unlicensed activity and violates the escrow agent licensing requirements. Licenses not renewed within 60 days, rather than one year, after the renewal date are canceled.

The subject matter that the examination is required to cover, and the requirement that the examination be given annually are deleted.

Bonding.

Required fidelity bonds must provide fidelity coverage for any fraudulent or dishonest acts committed by corporate officers, partners, solo practitioners, escrow officers, and employees of the applicant engaged in escrow transactions. The bond is for the benefit of the harmed consumer if a corporate officer, partner, or solo practitioner commits a fraudulent or dishonest act. An escrow agent's bond must be maintained until all accounts have been reconciled and the escrow trust account balance is zero.

In the event that fidelity coverage is not available for any fraudulent or dishonest acts committed by corporate officers, partners, solo practitioners, escrow officers, and employees of the applicant engaged in escrow transactions, the applicant must file and maintain a surety bond in an amount the DFI deems adequate to protect the public interest. The bonding requirement is established in rule as a range of bond amounts between \$20,000 and \$250,000 that vary according to the average monthly balance of client trust funds of the applicant. The bond runs to the state as obligee, and runs to the benefit of the state or any person who suffers a loss because of a violation of the licensing requirements.

Prohibited Activities.

Prohibited activities are added. Escrow agents must comply with the requirements of applicable federal or state laws. They are also prohibited from collecting a fee for tracking unclaimed funds unless it is a bona fide out-of-pocket expense, or converting unclaimed funds for personal use.

A licensed escrow agent may not employ a person who:

- handles escrow transactions who has been convicted of, or pled guilty or nolo contendere to, a felony or gross misdemeanor involving dishonesty within the previous seven years; or
- receives money for trust accounts, disburses funds, or acts as a signatory on trust accounts if the person has shown a disregard in the management of his or her financial condition in the last three years.

Enforcement.

In addition to or in lieu of a license suspension, revocation, or denial, or fines payable to the DFI, the DFI may order an escrow agent, officer, controlling person, director, employee, or licensed escrow officer to make restitution to an injured consumer.

The DFI may immediately take possession of the property and business of a licensee if it appears that, as a result of an examination, report, investigation, or complaint:

- the licensee is conducting its business in such an unsafe or unsound manner as to render its further operations hazardous to the public;
- the licensee has suspended payment of its trust obligations; or
- the licensee neglects or refuses to comply with any order of the DFI unless the enforcement of the order is restrained in a proceeding brought by the licensee.

The DFI director (director) may retain possession of the licensee's property and business until the licensee resumes business or its affairs are finally liquidated. The licensee may only resume business upon terms the director prescribes.

During the time that the director retains possession of the property and business of a licensee, the DFI may conduct the licensee's business and take any action on behalf of the licensee that the licensee could lawfully take on its own behalf, including discontinuing any violations and unsafe or injurious practices, making good any deficiencies, and making claims against the licensee's fidelity bond, errors and omissions bond, or surety bond on behalf of the company.

The director, the DFI, and its employees are not subject to liability for these actions and no moneys from the DFI's fund may be required to be expended on behalf of the licensee or the licensee's clients, creditors, employees, shareholders, members, investors, or any other party or entity.

Substitute Bill Compared to Original Bill:

The collection of payments and the performance of related services by a third party in connection with a loan secured by a lien on real or personal property is removed from the definition of "escrow."

Appropriation: None.

Fiscal Note: Available.

Effective Date of Substitute Bill: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) This is a great consumer protection piece of legislation. It recognizes the very important role of escrow agents in major financial transactions and adds many needed protections for consumers. The DFI did extensive stakeholder work with the escrow industry. This has been one of the more productive stakeholder groups. Stakeholders are in agreement that there needed to be some clean-up to the escrow statutes.

The DFI has received numerous complaints this year with over \$1 million in lost client funds. Under current law, a company with significant violations goes into receivership with very little legal authority. This bill allows the DFI to take over the company and keep running it so consumers can be properly protected. The DFI has also received numerous complaints against attorneys and this bill clarifies the DFI's regulatory authority over those who principally serve as escrow agents.

The bill requires that in addition to the escrow agents already covered, owners also need to be covered by a fidelity bond. Most escrow companies already have this bond. The remaining that do not are hoping that this fidelity bond will be available. Support of this provision by the escrow industry is dependent on the fidelity bond being actually available.

A few companies would be regulated by this act that are not already covered. No other form of regulation currently covers them.

(Opposed) The new definition for "escrow" in this bill covers businesses that perform contract collect services and are very different from a traditional escrow company. These companies should not be included in the bill, and the definition of "escrow" in the bill should be restored to the definition under current law. They do not belong in this regulatory structure. This would require agents of these companies to take irrelevant training and examinations. Data processing services companies should also not be regulated under the escrow statutes. It would be alien to the business structure of these companies. If they do need to be regulated, the licensing requirements should be different.

This bill was done without input from stakeholders. It is unclear whether the fidelity bond will be available for small companies and this could put escrow companies out of business. The bill also gives the DFI too much authority to take over companies at will and then not make them liable. This authority is too open-ended and does not define in what situations it applies.

Persons Testifying: (In support) Representative Nelson, prime sponsor; Deb Bortner, Department of Financial Institutions; and Tammie Warnke, Phil Dryden, and Dee McComb, Escrow Association of Washington.

(Opposed) Warren Tessler, Trust Accounting Center; Eric Johnson, Automatic Funds Transfer Services; and Dennis Daus, Seatac Escrow, Inc.

Persons Signed In To Testify But Not Testifying: None.