



Earnest Money and Escrow

(From the first check to the last!)

by

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This 5-clock hour course will cover the handling of the earnest money, the escrow process, the breakdown on the settlement statement, and challenges that can delay closing residential transactions.

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Clockhours by Mail

1. You will be provided with a booklet of with the class material. The material is the property of Professional Direction. This is one section of the Advanced Real Estate Practices Class
2. The course has been divided up into one-hour sessions. In Washington State a “clock hour” is 50 minutes. There are questions about each session. They can be answered while reading the material, at the end of the session, or at the end.
3. ***Answer*** the questions in the Workbook and complete the final test..
4. If you have any questions regarding the material or the questions, don’t hesitate to call or email Natalie Danielson.
5. ***Email*** Workbook answers and Evaluation to Professional Direction.
6. The certificate will be mailed probably within HOURS depending on the time of day, etc.!!!!

Disclaimer. The course materials and questions are not to be used for legal advice. Information can change over time. Real estate transactions are handled different ways in different regions in the State of Washington. If you have any comments or concerns about the material contact Professional Direction.

Thanks!

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Earnest Money and Escrow

From the first check to the last Curriculum

Chapter Hours	Major Topics	Method of Instruction
1 1 hour	1. What is Escrow? Define escrow in Washington State. Learn the purpose of the escrow process. Discover a typical escrow schedule.	Read Material Answer quiz
2 1 hour	2. What is Earnest Money? Define Earnest Money. Understand the proper handling of earnest money.	Read Material Answer quiz
3 1 hour	3. From Agreement to Escrow Understand the importance of escrow instructions. Become aware of some of the problems. that occur during the escrow process.	Read Material Answer quiz
4 1 hour	4. Closing Challenges Identify problems that can occur before and during closing.	Read Material Answer quiz
5 1 hour	5. Closing Documents Understand the entries as debits or credits. Know the information on the new CFPB changes. Understand the 3-day review.	Read Material Answer quiz

Earnest Money and Escrow

From the first check to the last

When a seller and a purchaser come together to transfer ownership of real property in Washington State most often the transaction is closed with the services of escrow. As a real estate licensee, it is important to understand the process of closing a transaction and the services provided by a neutral third party.

Course Objectives

As a result of taking this class the real estate licensee shall be able to:

- Define “Escrow” in Washington State.
- Understand the escrow process and a typical schedule.
- Identify the information that is necessary to create escrow instructions.
- Define “Earnest Money”
- Identify the different forms of earnest money.
- Understand the proper handling of earnest money.
- Know some of the problems that can occur during escrow.
- Estimate the closing costs for seller and purchaser.
- Show how taxes and insurance are handled at closing, including proration, prepayment, and reserve accounts.
- Explain how closing dates and different financing methods affect closing costs.
- Know the new CFBP changes and forms.
- Understand the requirement for a 3-day review of Closing Document

1. What is Escrow?

An escrow is a method of closing in which a neutral third party is authorized to act as escrow agent and coordinate the closing activities. The escrow agent holds monies and legal documents on behalf of the buyer and seller and handles them according to their instructions in order to close or complete the sale.

Under the Washington Escrow Agent Registration Act, escrow is formally defined as:

"Any transaction wherein any person(s), for the purpose of effecting and closing the sale, purchase, exchange, transfer, encumbrance or lease of real or personal property to another person(s), delivers any written instrument, money, evidence of title to real or personal property, or other thing of value to a third person to be held by such third person until the happening of a specified event or the performance of a prescribed condition(s), when it is then to be delivered by such third person in compliance with instruction under which he is to act, to a grantee, grantor, promisee, promisor, obligee, obligor, lessee, lessor, bailee, bailor, or any agent or employee thereof."

Who can close transactions in Washington?

Washington's Escrow Agent Registration Act requires escrow agents to be licensed and registered with the Department of Financial Institutions (D.F.I.). There are a number of exemptions from these requirements, however. Attorneys, title companies, banks, savings and loans, credit unions, insurance companies, and federally approved lenders are allowed to perform escrow services without being licensed or registered under the act. In addition, those acting under the supervision of a court such as receivers, trustees in bankruptcy, guardians, executors, and probate administrators.

Can a real estate broker close one of their transactions?

In Washington State a broker handling escrow for their own transactions is also exempt from licensing, provided they do not charge a fee for their escrow services. Very few brokers will ever close real estate transactions because of liability issues.

For a company to be licensed as a Certified Escrow Agent to engage in the escrow business under the registration Act it is necessary for a partner or corporate officer to pass an escrow agent examination, pay a fee, submit affidavits of good character, present a good credit report and obtain a fidelity bond. The certified escrow agent may employ Escrow Officers to close transactions and they must also be licensed.

A "Closer" is someone who works for an escrow agent. The term "L.P.O." is short for Limited Practice Officer, a person who has been authorized to prepare certain closing documents and perform routine closing functions under rules approved by the Supreme Court of Washington. A closer may or may not be an LPO. Different laws govern the conduct of different classes of Escrow Agent.

Who does the Escrow Officer Represent as an agent?

The escrow agent is a special agent for both parties and acts in accordance with the escrow instructions given by both. The escrow agent is a neutral third party who does not represent anyone in the transaction. If a party has a question about any aspect of the transaction, he or she should consult his or her own attorney for advice. Because of the escrow's limited duties of disclosure and the confidentiality of the escrow in general, facts known to the escrow holder are normally not imputed or implied to the other party. The escrow agent is a limited agent for both parties. Once the conditions to the escrow transaction have been performed, the nature of the dual agency changes. Escrow then becomes the agent for the seller for the money and the buyer for the deed. Escrow acts as the "clearing house" for the details of the transaction.

Who does the Escrow Office answer to?

The purchase and sale agreement serves as the primary escrow instructions for both the seller and the buyer. It should contain the agreement of the parties as to who pays for what expenses, proration dates, closing dates, etc. In the event of a disagreement, the escrow can only be amended, changed, or revoked by mutual agreement of the parties to the escrow.

Escrow is not to be negotiating or preparing real estate purchase and sale agreements. They are a neutral third party that uses the agreements to create instructions.

Can the Escrow officer prepare an addendum for the extension of the closing date or to authorize a credit to the buyer for a new exhaust fan if the agent assures him that all parties agree?

NO, the escrow officer is a neutral third party. They are not real estate licensees. There are times that the escrow will agree to prepare such documents but the real estate agent should be aware that it is not in the scope of their responsibilities!

The escrow agent is not authorized to comply with any instructions or demands of any third person who is not a party to the escrow.

Can a broker demand that the escrow agent release his commission?

The escrow agent can only close the transaction according to the instructions given. A broker is a third party and not a party to the escrow, so he, therefore, cannot give instructions to the escrow agent.

The Escrow Process

1. After a purchase and sale agreement is signed escrow is opened. The escrow agent gathers the information necessary to execute escrow instructions.
2. A Commitment for Title Insurance is ordered by escrow. Most of the time preliminary titles have been ordered by the listing agent and escrow contacts the title company for an update, which will include a search on the purchaser's name. The preliminary title will identify the property and any clouds on the title including liens, mortgages and deeds of trust, homeowners' association, CCR's, etc.
3. The escrow agent holds monetary deposits for the buyers in a trust or escrow account. Only a few of the real estate selling offices hold earnest money funds for the buyers in the real estate brokers trust account. Escrow verifies all the deposits made for the buyers.
4. Buyer and seller deposit all pertinent documents and other items with the escrow agent before the specified date of closing.
5. The escrow agent examines the title to determine whether there is marketable title and to identify liens that must be paid from closing funds. Escrow orders payoff figures from any lien holders. The seller may have one or more deeds of trust that need to be paid. There may be other liens including a leased fixture or judgment.
6. The escrow agent prepares the documents, such as the deed for closing.
7. In the event of a FHA, VA or Conventional financing, the lender prepares the purchaser's Closing Disclosure and the escrow agent prepares the seller's closing disclosure. Any other loan type, Escrow, prepares both purchaser's and seller's closing statements. Escrow determines how the funds are allocated based on the agreements and the liens. The commission is determined based on the commission disbursement statement provided by the agents. Commission is paid only to real estate brokers and not the individual real estate agents.
8. The escrow agent meets with the buyers and the sellers to sign the closing documents. The buyers and the sellers can meet separately with escrow for signing. The documents can also be sent to the buyers and sellers for signing. Typically, the seller's signing appointment can take between 10-15 minutes and the purchaser's signing appointment can take 30-60 minutes, depending on the number of documents and questions.
9. The documents are either returned to the lender for final review or scanned to the lender.
10. After the lender review the documents, they then contact the Escrow to "balance" which would be the amount wired to Escrow to complete the transaction. After the wire is received by Escrow, the escrow agent sends the documents to the title company for recording.
11. Once the documents are recorded the funds are dispersed. At that time the transaction is "closed."

Opening Escrow

Kristen and Joseph Archival write up an offer on a property in Kirkland, Washington with their Real Estate Agent, Ricardo at Our House Realty. The Seller signs the offer and the offer is delivered back to the agent for the Archivals on May 20th.

Agreement occurs in this situation when a signed copy of the offer is delivered back to the Archivals or to their agent.

The earnest money check is deposited within 24 hours as per the agreement.

The Archival's have requested Home Title Insurance Company and Black Pen Escrow.

Ricardo, the agent, delivers the Purchase and Sale Agreement to Black Pen Escrow Company. Escrow is opened.

Black Pen Escrow begins to gather the information necessary to close the transaction. This information includes:

- The condition of the title from the Title commitment ordered from Home Title Insurance Company
- The Seller provides the Loan pay off information and other information on lien holders.
- The verification of the earnest money deposit from Our House Realty
- The loan information from the lender chosen by Archivals.
- The commission information from the Listing office and Selling office.

Real estate agent responsibilities

Get ALL the pages of the purchase and sale agreement to Escrow.

Forward ANY addendums or changes made on the contracts after Escrow opened.

Communicate with the Clients, Lender, Title, and Escrow regularly.

Real Estate Agents must NOT do the following!

Do not ask Escrow to write up addendums! (For any reason!)

Do not ask for commission prior to closing or to be paid directly to agent.

Do not tell a buyer or seller their "legal rights" especially when there are problems.

2. What is Earnest Money?

Earnest money is sometimes referred to as a good faith deposit, binder, or deposit. It is evidence that the purchaser intends to carry out the terms of the contract in good faith.

In Washington State it is NOT required for the purchaser to pay earnest money when making an offer on a property.

Amount of Earnest Money

The amount of earnest money is not set by any laws or rules. The amount of the deposit is a matter to be agreed upon by the parties. The amount should be an amount that will:

- Discourage the buyer from defaulting or not completing performance on the contract.
- Compensate the seller for taking the property off the market,
- Cover any expenses the seller might incur if the buyer defaults.

The earnest money can vary in different regions based on the sales price of the properties, the type of financing, and/or the amount of time the property will be off the market before closing.

If the average home sells for \$100,000 in one city and in another city the homes are selling for over \$500,000, the amount of earnest money that is agreed upon will vary. Some agents have used 3%-5% of the sales price for the earnest money deposit.

On the other hand, if the buyer is obtaining financing for a property that is only \$100,000 with a zero down VA loan, then sometimes the earnest money deposit is lower because their cash funds are limited.

Forms of Earnest Money

The purchaser can deposit earnest money in a variety of forms. It is most common for the buyer to write a personal check that is deposited into an escrow or trust account until closing.

The form of earnest money shall never be changed by the real estate licensee. If the buyer has cash they want to use for earnest money and the seller agrees, the agent cannot deposit the cash into their personal account and then write a personal check for the same amount.

Personal Check, Cashier's Check, Money Order, Certified Check

Most earnest money is paid in the form of a personal check from the purchaser. It is deposited into a trust account at the real estate firm or the closing company. The check is made payable to the company where it is to be deposited.

If the purchaser is from out of the area, often the broker will suggest that the earnest money be paid in the form of a cashier's check or wire.

Wire Transfer

The purchaser can often have the earnest money wired from the bank. Make sure the information and wiring instructions are communicated directly from the escrow because this is a large area of fraud. Hackers can intercept emails and change wiring instructions.

Cash

Cash cannot be accepted in a real estate transaction. It is best to advise your clients to obtain a cashier's check or a personal check.

Promissory Note

When a buyer does not have their checkbook, is short of funds at the time of signing a purchase and sale agreement or does not want to deposit earnest money until certain conditions are met, then they might choose to write a promissory note. The note is a "promise to pay" by the purchaser. It is very important as the agent to make sure that the promissory note is turned into a check and deposited into the trust account when due. The challenge is that they are often very difficult to collect should the buyer default. It is recommended that the promissory note be payable on a specific date and NOT be made "payable at closing." The closing date may change or the closing may not happen due to default by the purchaser. Then, the promissory note is often not collected. The note shall be made payable on or before a specified date.

Other Forms of Earnest Money

There are times that the purchaser requests to offer stocks, bonds, cars, or jewelry as earnest money for a real estate transaction. If the seller accepts another form of earnest money other than cash, the item must have a stated value. The purpose of earnest money is to show the buyers good faith in purchasing. If the buyer defaults, the buyer could stand to lose the earnest money in whatever form agreed. The seller must agree and have knowledge of any item other than check accepted for earnest money.

No items of value or cash can exchange between parties outside of the real estate documentation.

Depositing Earnest Money

A real estate broker is not required to have a trust account. In fact, only approximately 30% of brokers have one. Without a trust account, the earnest money is deposited into an escrow trust account. The broker is to maintain records regarding the receipt of the earnest money by the escrow company.

Handling Earnest Money

The real estate commission in 2003 identified a common problem area in the handling of earnest money. Some brokers or agents were allowing the buyer to deliver the earnest money to the closing agent. In some cases, this caused problems in that it was only later in the transaction that the listing agent or seller found out the delivery was either not made or the delivery was late, which could have been detrimental to the seller. The new change prohibits a buyer from delivering the earnest money to the closing agent and makes the broker responsible for timely delivery. The change did not affect the requirement for the broker to secure a receipt from the closing agent.

Nearly every real estate purchase and sales contract has the phrase or a phrase like “time is of the essence.” The late delivery or deposit of earnest money may be very critical to the consummation of the transaction. Please remember that brokers are always responsible for the safeguarding of client funds.

WAC 308-124E-110(4)

(4) When a transaction provides for the earnest money deposit/note or other instrument to be held by a party other than the firm, a broker shall deliver the deposit to the designated broker or responsible managing broker. The designated broker will have the ultimate responsibility to deliver the funds. A dated receipt from the party receiving the funds will be obtained and placed in the transaction file.

WAC 308-124-205(4)

(4) Where an agreement for the sale of real estate has been negotiated involving the services of more than one licensee, and funds are to be deposited by the purchaser prior to the closing of the transaction, the firm first receiving such funds shall retain custody and be accountable, until such funds are distributed or delivered in accordance with written instructions signed by all parties to the transaction.

If the earnest money is deposited with the escrow office, they have different business practices than what is contracted in the purchase and sale agreement. For example, the escrow office may deposit the earnest money check upon receipt even though the purchase and sale agreement state it shall be deposited upon satisfaction or waiver of the home inspection.

It is important to make sure that as an agent you are accountable for all earnest money checks. Each office has procedures for the receipt and deposit of the check. In addition, if the buyer’s offer is not accepted, the agent has the responsibility to return the check to the buyer immediately.

The earnest money is held by a third party in a broker, escrow, or attorney trust account. It is written on the purchase and sale agreement the place that the earnest money is held and when it is to be deposited.

If the earnest money is held in the broker’s trust account full and accurate records are to be kept by the broker and audited by the Department of Licensing. The earnest money is not to be commingled with the broker’s own personal or business funds. If the broker uses the earnest money funds for his or her personal use it is called conversion and a violation of the Washington State Trust Account laws.

Interest from Deposited Earnest Money

The interest from the broker's trust account is transferred into the Washington Housing Trust Fund. If the earnest money exceeds \$10,000 the purchaser can elect to have the money held in a separate trust account and keep the interest less any bank charges.

If the earnest money is held in the trust account of an escrow office or title company, then the real estate agent for the buyer shall have a copy in the transaction file of a dated receipt when the deposit is made. This is required by the Department of Licensing.

If the purchaser writes a post-dated check this must be disclosed to the seller. The broker may have a policy against accepting postdated checks. The check must still be turned over to the broker or the escrow office to be held.

Earnest Money Return to Purchaser

Because earnest money is held to show the purchaser's good faith in proceeding with the terms of the contract, the return of earnest money is determined on the reason for the termination of the contract.

Before a Binding Contract

Requests for the return of the earnest money any time before the offer is binding is acceptable. If the purchaser writes a purchase and sale agreement and the purchaser withdraws the offer before the seller has signed it, then the purchaser shall be entitled to the return of the earnest money check.

If the seller rejects the offer or signs a counteroffer that is not acceptable to the purchaser then the purchaser is entitled to the return of the earnest money.

After mutual agreement

Once the purchaser's offer has been accepted, both parties have an interest in the earnest money.

There are conditions that may have been agreed upon in the purchase and sale agreement whereby the purchaser may be entitled to the refund of the earnest money.

Examples include.

- The purchaser may not be able to obtain financing,
- The home inspection may have discovered problems that cannot be resolved and the agreement terminate,
- The purchaser has a contingency to sell their present home and was not able to do so,
- The seller could not provide clear title to the property, or
- The seller could not sell the property.

If one of these types of situations occurs, most often a rescission is drawn up by the selling agent and signed by all parties. That rescission is sent to escrow who will release the funds. If that is not an option, then it is important to go immediately to the broker to resolve any issue.

Disputes over Earnest Money if there is a Default.

The seller may be entitled or think that they may be entitled to part of all the earnest money if the purchaser defaults and fails to close the transaction as agreed. The buyer may be entitled or think they are to all of the earnest money if the buyer feels there are issues that stop the buyer from closing.

In 1991 the Legislature created a law governing earnest money deposits as liquidated damages. RCW 64.04.005 states:

A provision in a written agreement for the purchase and sale of real estate which provides for liquidated damages or the forfeiture of an earnest money deposit to the seller as the seller's sole and exclusive remedy if a party fails, without legal excuse, to complete the purchase, is valid and enforceable, regardless of whether the other party incurs any actual damages. However, the amount of liquidated damages or amount of earnest money to be forfeited under this subsection may not exceed five percent of the purchase price.

At the time of signing the purchase and sale agreement the buyer and the seller agree that either the earnest money that doesn't exceed 5% of the sale price is the sole remedy or that the seller can elect a remedy. This is called the "safe harbor clause."

The Northwest MLS Purchase and Sale agreement states regarding default:

"In the event buyer fails, without legal excuse to complete the purchase of the property, then the following provision shall apply:

I. Forfeiture of Earnest Money. That portion of the Earnest Money that does not exceed 5% of the purchase price shall be forfeited to the Seller as the sole and exclusive remedy available to seller for such failure.

II. Seller's election of Remedies. Seller may, at seller's option, (a) keep the Earnest Money as liquidated damages as the sole and exclusive remedy available to seller for such failure, (b) bring suit against buyer for seller's actual damages, (c) bring suit to specifically enforce this Agreement and recover any incidental damages, or (d) pursue any other rights or remedies available at law or equity."

If there is a default or the transaction fails to close, the parties must agree in writing who is entitled to the earnest money.

In April 2015 a new law regarding how disputes over earnest money on residential real property improved or unimproved was signed. Within 15 days from the receipt of a written demand from a party to the transaction, the holder must either: 1 Notify all parties of the demand, 2 release the earnest money to one of more of the parties; or 3 commence an interpleader action in Superior Court.

If the holder opts to notify other parties, the holder's notice must be in writing sent by US mail and email to the parties' last known addresses and include a copy of the demand. It must contain a statement that."

- The parties have 20 days from the mailing date of holder's notice to provide notice of their own objection to the release of earnest money; and
- Their failure to deliver a timely written objection within 20 days will result in a release of the earnest money to the party that made the original demand.

If the holder receives an objection within 20 days, it must file an interpleader action in Superior Court within 60 days of receiving the objection or an inconsistent demand. However, the holder may release the funds or delay filing the interpleader action if it receives consistent instruction to do so from the parties after their initial objections. If the holder receives no objections, it must deliver the earnest money to the demanding party within 10 days after the 20-day period expires. The holder may also file an interpleader action at any time, even if no conflicting demands were received.

If the holder of the earnest money follows the procedures outlined in the bill, it is not liable to any person for releasing the earnest money to the demanding party, unless it releases the funds on the initial demand without waiting for objections of filing an interpleader action.

An interpleader action is a lawsuit in which the holder of a sum of money deposits the money or property with the court and names as defendants the parties who assert rival claims to the money. The court then determines the ownership of the money or property and the original holder is absolved of responsibility.

Earnest Money Deposit

The Archivals write up an earnest money check in the amount of \$5000.00.

Ricardo, their agent, should remind them that when there is mutual agreement, the earnest money will be deposited into a trust account. (Many buyers are unaware that the money is deposited prior to closing.)

Ricardo's office, Our House Realty, does not have a trust account. So, Ricardo delivers the check to Black Pen Escrow the next day.

Ricardo must get a receipt from escrow to have in the office file as evidence that the check was deposited into Escrow.

Real estate agent responsibilities

- Deposit the check within 24 hours to the trust account.
- If the trust account is not at the real estate office, then get a receipt upon delivery.
- Do not take cash as earnest money.
- Do not deposit the earnest money into a personal account.
- Do disclose to the other party's agent if there is a problem with the earnest money.
- Do consult broker immediately, if the transaction is failing and a party is demanding the earnest money.
- If an offer does NOT get signed, return the earnest money check to the buyer. Do not keep it for the next offer.
- Do not advise the buyer or the seller who is entitled to the earnest money if there is a default and dispute over the earnest money.

3. From Agreement to Escrow

The Purchase and Sale Agreement

The escrow agent is bound by the terms of the Purchase and Sale agreement and may only carry out the terms of the contract while fulfilling escrow responsibilities. The escrow agent takes the escrow instructions from the Purchase and Sale Agreement. Incomplete or incorrect information on the Purchase and Sale Agreement can delay the closing or jeopardize the transaction. Often the Purchase and Sale agreement, if handwritten, is completely illegible!

The following items are commonly missing from Purchase and Sale Agreements and are necessary to close transactions.

- Copy of the entire Purchase and Sale Agreement including all addendums and counteroffers.
- The full name of the purchaser(s) and the seller(s).
- How the purchaser(s) intend to take title (as husband and wife, individual, joint tenants, tenants in common, corporation, partnership, etc.) You are not required to have this information and in fact, can only ask purchasers “how they take title” not “Are you married?”
- Property address
- Full legal description
- Method of payment
- Leased fixtures
- List of any personal property as a part of the sale
- Closing date
 - Make sure that it is definable and includes all extensions.
- Earnest money deposit must be verified.
- All conditions and repairs must be addressed.
- Signature of all parties. All documents must be signed and initialed by all parties.
- The names and addresses of all parties including the real estate agents.

Escrow Instructions

The escrow instructions should include the following:

- Identification of all documents placed into escrow.
- Identification of the source of the documents
- Tell me what steps or actions are required to be taken.
- Tell who is supposed to take such steps or actions.
- Notice to the escrow agent when actions are completed.
- Identification of what is to happen if required actions are not completed by specified date.

The escrow instructions should be able to answer the following questions:

What are the documents being used?

Who is the source of those documents?

What is to be done?

Who is supposed to do whatever is to be done?

When is to be done?

What is to happen if things are not done when they are supposed to be done?

Can the escrow instructions modify or amend the Purchase and Sale Agreement?

No. The escrow instructions are not to change the agreement. The agreement is what the escrow instructions follow.

The Closing Documents

The Warranty Deed transfers ownership.

Final Escrow Instructions are completed.

The Excise Tax Affidavit verifies that the excise tax is paid.

Loan Documents for the borrower's loan.

Lien Release Documents are from the seller's lender releasing the prior lien.

Holdback Agreements are signed if there is money to be held by escrow to pay for or assure that a cost is taken care of. For example, a holdback could be done to cover the cost of replacing an appliance that has not been delivered.

Signing Documents

The escrow agent is responsible to secure the signatures of the parties on the Closing Documents.

Which documents require "Original Signature"?

The recorded documents and Power of Attorney

Which documents does the escrow closer get signed?

Everything

Which documents does the loan officer get signed by the purchasers?

The original loan application and good faith estimate

Who signs a partnership? A corporation?

It depends on the agreement and who is authorized to sign on behalf.

How does the escrow agent identify the parties?

They are required to provide identification with picture and signature.

Disbursement of Funds

Escrow is responsible for disbursing the funds to close the transaction. Escrow therefore:

Receive loan proceeds from lender.

Makes the payoffs on underlying liens.

Pays the real estate commissions to the broker of the real estate firm.

Disburses to the seller the proceeds from the sale.

Pays title insurance and recording charges.

Credits the buyer with any funds as specified in the agreement.

Pays the costs for the transaction through credits and debits on the settlement statement.

Pays any other charges or holds funds in reserve for final bills.

Collects the escrow fee.

Disburses any holdbacks to holdback accounts.

Real Estate Agent Responsibilities

What can the Real Estate Agent do to get those transactions closed???

A real estate agent can contribute to a successful real estate closing. Some errors and problems that occur can delay or contribute to the failure of a closing. Real estate agents can help by remembering the following ways to stay on top of the transaction.

Prepare a LEGIBLE, if handwritten, purchase and sale agreement

Too often the escrow or closing agent cannot read the handwriting on the purchase and sale agreement. Errors can occur when translating the agreement into escrow instructions.

Get all signatures and initials on any changes to the agreement.

It is important to make sure that all parties sign everywhere required on the purchase and sale agreement.

Have the power of Attorney reviewed by escrow so they can get title to approve it.

Make sure that you get a copy of the Power of Attorney to Escrow PRIOR to signing any contracts. The Power of Attorney your client has may not be acceptable!

Forward copies of all addendum's, extensions, and changes to escrow

The additions and changes to the purchase and sale agreement must be forwarded to the escrow closing agent immediately. Those changes affect the instructions and often the bottom line. There are times that agents forget to forward changes in sales price causing quite a problem when the parties are signing at closing.

Handle promptly all problems that occur that involve the agent, including work orders and inspections.

Time moves quickly and it is important to attend to problems and conditions that must be met as soon as possible. Procrastination, often, is the only reason many transactions do not close on time.

Include all costs or credits in the purchase and sale agreement.

The settlement statement must include all the costs and credits so that the figures are in balance at the time of closing.

Provide escrow with commission instructions that are detailed by submitted a Commission Agreement Authorization form.

The commission paid to the real estate agents must be clear to the escrow closing agent. A commission disbursement form should be forwarded to Escrow to insure that the commission is paid to the real estate offices.

From Agreement to Escrow

The purchase and sale agreement can be unenforceable without a legal description. It is best to include the legal at the time the purchase and sale agreement is written. The agreement does state that the closing agent can insert the legal description. The real estate broker calls the Title Insurance company for a copy of the legal description.

Escrow needs the full names and addresses of all the parties and sends them a letter acknowledging that escrow has opened and verifying addresses and sends out their closing instructions to be signed and returned.

The parties may have had a home inspection and renegotiated the purchase price due to several repairs. The addendum reducing the price must be forwarded to the Escrow Company.

The lender needs more information to process the loan. The closing date has been extended three additional days. The real estate broker writes up an addendum to extend the closing date, gets the signatures of the parties, and forwards it to Escrow.

The lender provides loan information and often documents when the loan has been approved.

Escrow draws up the documents to close including the deed and excise tax affidavit.

Escrow prepares the Settlement Statement or Closing Disclosure depending on the type of loan transaction.

Escrow calls the Sellers and Buyers to make appointments to sign the documents.

The documents are returned to the lender or scanned to the lender based on their instructions for final review.

The loan is funds wired by lender and received by Escrow.

The transaction is recorded in the county.

The funds are available to the seller and all disbursements are made.

The keys are given to the Buyers.

4. Closing Challenges

What is Closing?

The closing of a real estate transaction in Washington State occurs when the documents are signed and recorded and the funds are available to the seller. The closing date is the day the buyer takes ownership. Possession occurs when specified in the purchase and sale agreement.

The parties to the transaction usually sign 24 hours before the actual closing. At that time the documents are all drawn and signed. At this time any final money owed as part of the transaction is paid by cashiers check or wired funds.

Title Insurance

The escrow agent orders the Preliminary Commitment for Title Insurance. The type of insurance coverage is specified in the Purchase and Sale Agreement. With a title insurance policy, the title insurance company agrees to indemnify the policy holder against any loss caused by defects in the title. A defect in the title could include a forged deed, clerical errors, or a deed executed by a minor. There are specific defects that are excluded from coverage. An example would be a loss a homeowner might incur due to a zoning change.

Clearing Clouds

During the escrow period often there can be clouds that appear in the title. These clouds can delay or even stop a closing on the property. A preliminary title report is ordered at the time escrow is opened. Sometimes the preliminary title report is ordered with the listing and updated at the time escrow is opened. The preliminary title report can identify some problems or clouds on the title.

Problems with the Parties

- The seller or buyer may have a common name. They will be required to sign an “Identity Affidavit.”
- Judgments or tax liens against the seller or the property
- Judgments or tax liens against the buyers may have to be cleared by their lender.

Problems with the Property

- There may be a missing link in the chain of titles.
- Discrepancies in the legal description
- Unplatted lots
- Encroachments
- Easements
- Restrictive covenants
- Ingress and egress problems
- Right of first refusal
- Restrictions on the right of sale (due on sale)
- Reservations and Mineral, water, or development rights

- Adverse possession rights
- Land use and zoning restrictions
- Existing assessments on the property
- Environmental problems

Hidden Defects

Some of the most serious risks are not revealed by the records or by an examination of the title. Sometimes during escrow these unresolved issues from the past could surface. They are usually covered by a title insurance policy but not always. They include the following.

Marital Status of the Owner Incorrectly Given

One spouse may have an interest in property owned individually by another spouse. An owner may say that he or she is single, although secretly married or perhaps married/divorced in another state. This could result in a claim by a spouse or former spouse whose existence was not suspected. “Hey there! I own half of that house!”

Undisclosed Heirs

When an owner dies interstate where there is no will, the courts must decide who the rightful heirs are. But, even then, such a decision by the court may not be final or binding on any heir who was not notified of the proceeding. Even under a will, the court may have to settle questions on interpretation of the will. Examples include children born after the date of the will and heirs overlooked due to incorrect probate proceedings. “Wait! What about my baby?”

Mental Incompetence or Minors

A transfer of property by a minor or a person adjudged to be mentally incompetent raises special problems. To be valid and binding on a minor or incompetent, the transaction must be made by guardians or conservators appointed by the court. If a deed was executed by a person who was a minor or under mental disability at the time, the transaction may be voidable or invalid. “My uncle was crazy when he sold the house!”

Fraud and Forgery

Fraud or forgery will not be shown as a matter of record. “That is ‘my’ house! Who are you?”

Examples where the title insurance company protects the new owner include:

- A previous owner may have been fraudulently impersonated.
- Deeds, releases, mortgage, or other documents may be forged.

Defective Deeds

The deed may be defective for several reasons that may not be found in the title search.

Examples include:

- A deed may have been delivered without consent of the owner or after their death.
- A deed may have been executed under expired power of attorney.
- The name of the grantee may have been inserted in the deed after its delivery.
- The officer or a corporation may not have been properly empowered to act.

Confusion Due to Similar or Identical Names

Despite a careful investigation to prevent it, some confusion of identity is possible.

Examples include:

- A person's title to his or her land, established thirty years ago may be under one name and the taxes may still be paid under the name... but the lawsuits, marriages, divorces, wills, and other actions may be under a simplified family name.
- Two members of the same family might have the same name as in the case of father and son.

Clerical Errors

Clerical mistakes are infrequent, but they do happen. A document may be missed in searching or entries in records maybe in error i.e. the parking or storage space number for a condo.

Items Not Covered by Title Insurance

These items may have to be dealt with, paid, disclosed and/or could interfere with the closing of a transaction.

Easements

An easement is a right, by express or implied agreement, to make use of another's property in a specific manner. Commonly seen easements include those for utility and access purposes. Easements may be created by reservation, specific grant or on the face of a plat. Most often easements do not affect the closing.

Road Maintenance Agreements

A document recorded to indicate responsibility for maintaining access easements and private roads. Lenders need to be sure their security is accessible by a maintained road. So, during the loan approval and escrow process it may be discovered that an agreement must be drawn up between the seller and the neighboring properties.

Reservation

A clause in a conveyance document, which reserves a specific right to the grantor. A common reservation is that of mineral rights. It is very common for mineral rights to have been segregated from the fee title and they do not affect the closing usually.

Covenants, Conditions, and Restrictions

Most subdivisions recorded in the past twenty years have extensive CCR's recorded which affect the use of the property. Even older subdivisions commonly have use restrictions in place. The purpose is to protect the value of all the properties in the subdivision by prohibiting uses which may be undesirable. Restrictions may also be recorded against a single property reserved on a deed.

Agreements

Agreements may be recorded against real property in many situations. It is not uncommon to see recorded Indemnity agreements between municipalities and property owners. The city of Seattle Commonly records these when a portion of the sidewalk is used for a street café. Agreements may also be recorded to indicate non-protestation of LID to be formed at a future date.

Excise Tax

A transfer tax paid at the time of sale of real property. The tax is collected at the county level, with proceeds directed partially to the state and partially to the city in which the property is located. Local custom is that the seller pays the tax at closing.

County Property Taxes

The amount of property tax due to the county on an annual basis. The taxes are often prorated and paid at closing.

Assessments

Monetary liens placed against property by municipalities to pay for an area improvement.

Liens against a property

Deed of Trust

The most used financing document.

Mortgage

A security instrument more commonly used prior to the creation of the Deed of Trust.

Real Estate Contract.

A form of seller financing whereby the seller holds the title to the property and the buyer holds only the purchaser's interest in the property.

Judgment

The final determination by a court as the outcome of a monetary dispute. It attaches to all real property owned by the debtor and will show on title.

Mechanics Lien

A statutory lien which attaches to real property by those who provide labor or materials to that property.

Pending Divorce

If a property is to be sold or encumbered before a divorce is final both parties must sign the deed.

Pending Civil Action

Indicates a court action involving the property.

Bankruptcy

Indicates a pending federal bankruptcy filing that affects someone with a record interest in the property.

Probate

Indicates a pending action that involves this property. This must be investigated prior to closing.

Earthquake or Tornado

Damage to an improvement or land caused by fire, natural disaster or depreciation is not included in title insurance.

Government Regulations

Zoning changes or restrictions placed on the land after the closing are not covered by title insurance.

Indian Tribal codes or rights

They are not covered and may be shown on the title report.

Clearing Common Exceptions

Physical Encumbrances

This category includes easements, use restrictions and agreements. These will remain on title unless very specific steps are taken. To obtain a release of these items, you must obtain a written release in recordable form from the parties who currently benefit from the encumbrance. An easement may be released by the parties who have the right of its use. Agreements may be released by all parties to the agreement. Plat restrictions (C.C.R.s) may contain specific requirements within the document regarding release but may prove impossible to release if they were a requirement of the initial platting process. If you need to remove any of these types of items from title, be sure to contact your escrow agent and title officer early in the transaction. It would be wise to contact your title officer even before your purchase and sale agreement is signed if you anticipate removal of physical encumbrances as a condition of the transaction. Removal of these types of encumbrances are complicated and may require the involvement of attorneys for both the buyer and seller.

Excise Tax

Excise Tax must be paid at the time of transfer of title and is based on the monetary consideration of the transfer. King County will not record a deed until the tax is paid and the deed is stamped with an excise receipt number. Excise tax payment may not be required in a few circumstances, as provided by statute: transfer for love and affection only, assumption with no proceeds to the seller and court-ordered transfers being some possible tax-free transfers. These exemptions are currently under review by the legislature and may be waived in the future.

Deed of Trust

When a Deed of Trust is paid off the original note (marked paid), original deed of trust (with signed request for reconveyance) and a trustee's fee (usually about \$50) must be forwarded to the trustee named in the deed of trust. The trustee checks for partial reconveyances and assignments of interest before executing and recording the Full Reconveyance. Sometimes the original note or deed of trust may be lost prior to reconveyance. Contact your trustee for their requirements in this situation. They may accept a Lost Note and Deed of Trust Affidavit. They may also require additional fees to be paid. Many trustees will resign in such situations, in which case the beneficiary appoints another trustee.

Mortgage

The beneficiary of a mortgage will execute and record a Satisfaction of Mortgage upon final payment.

Real Estate Contract

When paid in full, the contract seller will execute a Warranty Fulfillment Deed which transfers title to the contract purchaser. This should be recorded by the purchaser. Sometimes these deeds are executed at the time of the original sale and held in "true escrow". Paying off a string of contracts may be one of an escrow officer's most challenging tasks. If one of the parties to the contract has died, the original deed may not be sufficient.

Financing Statements

Most financing statements have a section on which to indicate payment in full or part. When paid, the beneficiary will check this box and record the same as a Termination Statement.

Judgment

When a judgment is paid, the creditor's attorney must execute a Satisfaction of Judgment and file this with the court. Judgments and their Satisfactions are not recorded with the county auditor like most other documents but filed with the Superior Court. Sometimes a "common name" judgment will show on title. If this occurs, the title

insurer will note that it may not be the person in question and ask that an Identity Affidavit be executed by the party named and submitted to the title insurer for review.

Mechanic's Lien

Upon payment, a Satisfaction of Lien must be executed and recorded by the lien claimant. If a lien is not paid and no foreclosure is initiated, a mechanic's lien may be considered "out by time" in nine months.

Pending Divorce

Property may be sold or purchased by parties to a pending divorce. In a sale situation, both parties must sign the deed; unless there is a Property Settlement Agreement previously approved by the court and accepted by the title insurer. In the situation of a purchase, both parties may need to acquire title and then record a deed from the party who will not be in title. Call your title officer for more details. Each of these situations is unique and demands special attention.

Pending Civil Action

Most title insurers are not willing to insure title to property currently in litigation. Since many of these actions are for other than monetary consideration, the transaction may have to wait until the case is decided. Call your title officer early on to clarify these types of situations.

Bankruptcy/Probate/Guardianship

Property may be transferred out of these estates by following specific, statutory steps. The title commitment will indicate the status of the action and who is authorized to deal with the transfer. Call your title officer for further information.

Corporations/Partnerships

Title insurers must verify who is authorized to handle property transfers from these entities, and the legal status of the entity itself. The requirements will be shown in the preliminary commitment. These will likely include submission of Partnership Agreements, Articles of Incorporation, Minutes of Meetings and Signature Authorization. You will want to pay particular attention to these requirements. Do not assume someone else is dealing with them or that title insurer will waive them.

Extended Coverage

Your title commitment will indicate whether Extended Coverage matters have been cleared. If there is a numbered paragraph showing "matters to follow by supplemental", make sure you check for that supplemental in a few days. The supplemental will either clear this item or set up specific requirements for its clearance. The most common item to show is "unrecorded lien rights" for recent work done on the property. Title insurers will clear this exception upon review and approval of a signed Builder Indemnity and Financial Statement. If other inspection items show, such as encroachments, call your title officer for information on what may be required for clearance.

Notes

Notes will be automatically removed prior to policy issuance, as they are for information only.

Remember to carefully review your title commitment upon receipt. All exceptions to title are much easier to deal with at the start of a transaction than the day prior to closing! Show your client or customer that you are a professional by handling these concerns early on in the transaction.

Closing Challenges

Examples of situations that can cause a delay or problems with closing to the Buyers on a house.

- The title insurance report identifies another party by the same name that has several outstanding judgments against him. If the judgments are not that of the buyer, then they will sign an affidavit at escrow stating that fact to be sent to title to clear the judgments.
- The legal description from the title insurance report notes the lot as number 13 but the purchase and sale agreement states lot number 14. The legal description is correct. The purchase and sale agreement used the builder's flyer for the name of the plat and the lot but it was changed for marketing purposes over the years.
- The seller of the property has several tax liens that exceed the equity that was believed to be in the property. Therefore, the seller may have problems selling the property.
- The property shares a driveway with the property next door. The lender requires that the sellers provide the buyers with a written road maintenance agreement.
- The title search revealed a mechanics lien on the property. The lien was placed over 10 years ago and the electrician is no longer in business.

The real estate agents' responsibilities

Return the calls to the escrow office when there is a problem.

Communicate with all parties when there is a problem.

Cooperate with the escrow company.

5. Closing Costs and the Settlement Statement

For each transaction, the escrow agent prepares a Closing Document. It sets forth all the financial aspects of the transaction in detail. It shows exactly how much the buyer will have to pay at closing, and exactly how much the seller will take away from closing.

Seller and Purchaser Closing Costs

The seller and the purchaser have costs to close the transaction. No two transactions are the same. In addition, many of the costs are based on the sales price. There is no rule that requires certain costs to be paid by certain parties. Most of the costs can be negotiated. The closing table is too late to negotiate costs to close!

Prorating Costs

Certain expenses are paid over a period. The total expenses for taxes, insurance and interest have to be prorated so the buyer pays their share and, in turn, the seller pays his share based on the actual day of ownership.

It is important to understand how costs are determined and prorated. Most often if there is any concern, one quick call to the escrow or closing agent will result in the total costs for the purchaser and seller.

Real Estate Taxes

Real estate taxes are paid to the county twice yearly. The first half of the year is paid by the end of April and the second half paid by the end of October. When the transaction closes the taxes are prorated so that one party is often reimbursed for taxes that have already been paid. The total tax bill for the year is divided by the number of days in the year (365 days.) To prorate the taxes, take the total amount of taxes divided by the number of days in the year arriving at a daily figure for the taxes. Then, determine the number of days that each party is responsible for the taxes.

EXAMPLE:

The annual tax bill for a property is \$1250.00. The closing date is May 23rd.

\$1250.00 divided by 365 days equals \$3.42 per day.

The seller owns the property from January through May 22 or 142 days.

The purchaser will own the property from May 23 through Dec 31 or 223 days.

The taxes were paid on April 30 for the first half of the year by the seller. So, the seller must be reimbursed for the taxes from May 23 through the end of June or 39 days. The seller would receive a credit for \$3.42 per day for 39 days or \$133.38.

Property Insurance

Property insurance is most often an annual premium paid at the date of closing. So that when the property sells, most often the seller is reimbursed for property insurance already paid.

EXAMPLE:

If the seller purchased the property on March 20, then the insurance is often paid annually on that date. If the closing is to occur on May 23rd, the seller will get a refund for the amount paid from May 23 through March 19th. If the insurance for the property is 350 per year, then the amount of insurance per day would total \$.96 per day. Take the amount of days between closing and premium renewal (300 days) and multiply by the amount per day \$.96 for a proration or credit to the seller of \$288.

Accrued Interest

Mortgage interest is paid in arrears rather in advance. To better understand this, think of it as the opposite of a rent payment. When a tenant pays rent, if it is paid on the first of the month it is for the coming month. If interest is paid on the first of the month it covers the previous month.

When a borrower pays interest on their loan it is often paid on the first of the month. So, if the transaction closes on the 15th of the month the seller will owe 14 days of interest at the time of closing.

The amount of interest would be prorated based on a 365-day (or in many cases a 360 day) year. Interest is determined daily. The number of days it is owned is then calculated.

The Closing Document

In August 2015 the Settlement Statement will now be known as the “Closing Disclosure” for FHA, VA and Conventional loans.

The items listed on the document are either debits or credits. A debit is a charge payable by a particular party. Credits are items payable to a party.

All the costs and fees are listed. This is the final place where all the debits and credits are balanced. The amount that is owed at closing is listed.

New Documents and Regulations that affect Closing.

The Dodd Frank Act required the Consumer Financial Protection Bureau (CFPB) to publish rules and forms that combine certain disclosures that consumers receive in connection with applying for and closing on a mortgage loan under the Truth in Lending Act (Regulation Z) and the Real Estate Settlement Procedures Act (Regulation X).

Effective August 1, 2015, the regulations, disclosures, forms, and documents will change for real property transactions with financing. It will not apply to home equity lines of credit, reverse mortgages, Mobile homes not attached to real property and a creditor that makes 5 or fewer mortgage loans in one year.

The **Loan Estimate** and **Closing Documents** will replace the Good Faith Estimate, Truth in Lending, and the HUD1.

The benefits of the new forms include:

- This will reduce paperwork by combining forms.
- Clear language will help consumers understand mortgage loans and real estate transactions.
- Information will be highlighted that is most important to consumers.
- More information about the costs of taxes and insurance is listed. How the interest rate and payments may change in the future will be listed.
- Warnings for consumers about features they may want to avoid like prepayment penalties.
- Cost estimates for services required to close will be more reliable.
- Require that the consumers receive the Closing Disclosure at least three business days before closing.

All the new forms and the regulations are available on the ConsumerFinance.Gov website.

Loan Estimate

This new form replaces the Good Faith Estimate and the initial Truth in Lending Disclosure. It must be provided to the consumer within 3 business days of applying for the loan. “Application” means the submission of a consumer’s financial information for purposes of obtaining an extension of credit. The LE provides a summary of key loan terms and estimate of costs for the consumer.

Closing Disclosure 3-day review

The consumer will have the right to review the terms of the transaction on new easier to use disclosure statements 3 days prior to closing.

If there are changes in the days leading up to closing that affect the basic terms of the transaction then the new regulations require an *additional* 3-day review. According to the CFPB on their website, the three changes that would trigger the additional three days include:

- a. The APR increases by more than 1/8 % for fixed rate loans or more than 1/4% for adjustable loans. A decrease in APR will not require a new 3-day review if it is based on changes to interest rate or other fees.
- b. A prepayment penalty is added making it expensive to refinance or sell.
- c. The basic loan product changes, such as a switch from fixed rate to adjustable interest rate or to a loan with interest only payments.

There has been much misinformation and mistaken commentary around this point, according to the CFPB. Any other changes in the days leading up to closing do not require a new 3-day review, although the lender will still have to provide an updated disclosure. For example, the following circumstances do not require a new 3-day review:

- a. Unexpected discoveries on a walk through such as a broken refrigerator or missing stove, even if they require seller credits to the buyer.
- b. Most changes to payments made at closing include the amount of the real estate commission, taxes and utilities proration, and the amount paid into escrow.
- c. Typos found at the closing table.

For more information on the 3-day review visit the [ConsumerFinance.Gov](https://www.consumerfinance.gov) website.

