

**DEPARTMENT OF BUSINESS OVERSIGHT***Ensuring a Fair and Secure Financial Services Marketplace for all Californians*

**Jan Lynn Owen**  
**Commissioner of Business Oversight**

IN REPLY REFER TO:  
FILE NO: PRO 13/13

September 22, 2017

**SECOND INVITATION FOR COMMENTS ON PROPOSED RULEMAKING UNDER THE  
ESCROW LAW  
(PRO 13/13)**

BACKGROUND

The Department of Business Oversight (“Department”) licenses and regulates escrow agents under the Escrow Law (Fin. Code, § 17000 et seq.). Under the Escrow Law, it is unlawful for an escrow agent to conduct business without first applying for and securing a license from the Commissioner of Business Oversight, unless the escrow agent is exempt from licensure.<sup>1</sup> The Department is considering changes to regulations that impact escrow agents. In accordance with Government Code section 11346.45, the Department is seeking comments from interested parties and those who would be subject to the proposed regulations prior to the Department providing notice of a proposed rulemaking action. The Department is seeking comments on amendments to section 1741.5 of title 10 of the California Code of Regulations (“Rule 1741.5”),<sup>2</sup> which interprets Financial Code section 17406 regarding the submission of an annual audit report. The Department is also seeking comments on the addition of section 1741.5.1 to title 10 of the California Code of Regulations (“Rule 1741.5.1”), which would interpret Financial Code section 17600 regarding conditions for the surrender of a license. The Department further is seeking comments on amendments to sections 1732.2 and 1737.3 of title 10 of the California Code of Regulations regarding escrow books and records to be maintained (“Rule 1732.2”) and preserved (“Rule 1737.3”).

On August 27, 2015, the Department sought comments from interested parties on amendments to Rule 1741.5 and the addition of Rule 1745.5.1. After receiving and reviewing comments from interested parties, the Department has incorporated many of the changes requested. The Department seeks the input of interested parties on the revised language.

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<sup>1</sup> Fin. Code, § 17200.

<sup>2</sup> Cal. Code Regs., tit. 10, § 1741.5.

## **Rule 1741.5 – The Annual Audit Report**

Existing Rule 1741.5 sets forth requirements for the content of the annual audit report that licensed escrow agents must submit to the Department and establishes additional procedures for independent accountants performing the audit. The amendments to Rule 1741.5 propose redrafting the existing rule to provide that the annual audit report would consist of two separate parts:

1. Audited financial statements and supplementary information, with an unqualified opinion of a certified public accountant (“CPA”) that the financial statements are fairly stated in all material respects; and
2. An agreed-upon procedures engagement, requiring the CPA to perform specified procedures, some largely equivalent to the procedures required under the existing rule, and defining the content of the report of findings.

The amendments also clarify the additional documentation required to be submitted with the report. The changes to the rule are intended to ensure that the attestations required as part of the annual audit report are consistent with the professional standards for CPAs.

By way of background, in early-2013 the Department identified some audit reports submitted on behalf of licensees that did not contain unqualified opinions regarding the audit reports submitted on behalf of licensees. In subsequent correspondence with licensees and their CPAs, the Department was advised that the CPAs would be violating their professional standards to provide opinions on audit procedures defined by a third party. To resolve this issue, the Department is proposing revisions to Rule 1741.5 to require an agreed-upon procedures engagement for a CPA to perform procedures that are specified in the rule.

Since the Department began developing new requirements for the annual report, the Auditing Standards Board redrafted the Statements on Standards for Attestation Engagements in SSAE No. 18, *Attestation Standards: Clarification and Recodification*. The proposed revisions to Rule 1741.5 incorporate the changes in SSAE No. 18.

### **Proposed Rule 1741.5.1 – Closing Audit Procedures**

The Department is also seeking comments on a proposed rule outlining procedures for a closing audit upon the surrender of an escrow agent license. Financial Code section 17600 authorizes the Commissioner to impose conditions on the surrender of a license. Under this authority, the Commissioner requires a licensee to submit a closing audit performed by a CPA to ensure that all escrow funds belonging to the public have been properly disbursed. Proposed Rule 1741.5.1 would require a licensee to enter into an attest engagement with a CPA to perform specified agreed-upon procedures intended to provide the Department with assurance that escrow funds were distributed properly and no funds were misappropriated.

## **Rule 1732.2 – Escrow Books, and Rule 1737.3 – Records to Be Preserved**

The Department is proposing changes to the rule that specifies the books that a licensee must maintain, and the rule that specifies the records to be preserved, to conform to changes proposed in the amendments to Rule 1741.5 and to modernize some outdated provisions.

### INVITATION FOR COMMENTS

In accordance with Government Code section 11346, subdivision (b), the Department seeks to involve parties who would be subject to the regulations and other interested parties in discussions regarding the proposed regulations. The Commissioner invites interested parties to review the accompanying draft text of revisions to the annual audit report required of escrow agents and the proposed closing audit procedures, and provide comments.

When the Department sought comments from interested parties on proposed language on August 27, 2015, the Department also requested interested parties provide information on the procedural and fiscal impact of the proposed changes. The Department again requests interested parties to address the following questions:

- How will the changes proposed in the text impact the actual audit procedures performed by CPAs?
- What fiscal impact is anticipated from the changes? If an increase in cost is anticipated, please specify the reason for the increase. Please estimate the cost impact that you expect from these changes.
- Do the changes proposed in the text raise any concerns regarding a CPA's ability to comply with professional standards? If concerns are identified, please specify any accounting rule, policy or statement that is implicated.

### TIME FOR COMMENTS

The Department is providing the attached text of draft regulations to interested parties, and invites interested parties to submit comments by **October 23, 2017**.

Comments from interested persons will assist the Department in determining whether amendments to regulations under the Escrow Law are necessary and appropriate. This solicitation for comments from interested parties is not a proposed rulemaking action under Government Code section 11346, and the public will have an additional opportunity to comment on proposed changes if, after consideration of the comments from interested parties, the Department proceeds with a notice of a proposed rulemaking action.

### WHERE TO SUBMIT COMMENTS

You may submit comments by any of the following means:

#### Electronic

Comments may be submitted electronically to [regulations@dbo.ca.gov](mailto:regulations@dbo.ca.gov). Please identify the comments as PRO 13/13 in the subject line.

#### Mail

Department of Business Oversight, Legal Division  
Attn: Mark Dyer, Regulations Coordinator  
1515 K Street, Suite 200  
Sacramento, CA 95814-4052

#### Fax

(916) 322-1559

### CONTACT PERSONS

Questions regarding this invitation for comments may be directed to Colleen Monahan, Senior Counsel, at (916) 323-7384 or [colleen.monahan@dbo.ca.gov](mailto:colleen.monahan@dbo.ca.gov).