

CALIFORNIA ADVOCATES, INC.



February 19, 2021

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BY ELECTRONIC SUBMISSION

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Department of Financial Protection and Innovation
Attention: Sherri Kaufman, Senior Counsel and Regulations Coordinator
300 S. Spring Street, Suite 15513
Los Angeles, California 90013

RE: Proposed Escrow Regulations (PRO 13/13)

Dear Ms. Kaufman and Regulations Coordinator,

The California Escrow Association (CEA) is a statewide association representing escrow professionals in California. Our members have a unique perspective on escrow issues because they provide services in escrow companies licensed by the Department of Financial Protection and Innovation, title insurers and underwritten title companies licensed by the Department of Insurance, and broker-owned escrow operations licensed by the Department of Real Estate. We appreciate the opportunity to provide comments on proposed regulations to the escrow law regulations noticed on January 4, 2021. It is our intention to supplement these comments with brief testimony at the public hearing on the proposed regulations scheduled for March 1, 2021.

As an association representing professionals in all entities authorized to provide escrow services in California, CEA has long been involved with proposed statutes and regulations within the subject matters of the current proposed regulations. For example, CEA partnered with the Escrow Institute of California and other stakeholders in helping craft and support SB 204 in 2009, which became Chapter 568, Statutes of 2009. This bill provided certainty and stability in assessments charged to licensed escrow companies by the Department, and added new provisions relating to the frequency and structure of annual audits performed by independent Certified Public Accountants. Prior to that, CEA worked with the California Land Title Association and California Association of Realtors on anti-rebate provisions relating to title insurers and underwritten title companies, eventually codified in Insurance Code Section 12404.

Because providers of escrow services in California are also regulated by the Department of Insurance and the Department of Real Estate, it is critical that DFPI regulations be considered in the context of the broader regulatory environment. Licensed escrow companies are almost entirely small businesses, often women and minority-owned, providing a very significant percentage of real estate, mobile home, and bulk transfer escrows in California. Therefore, regulations which have the effect of substantially increasing compliance costs, or which unreasonably restrain legitimate marketing and networking activities, could threaten this critical segment of the real estate industry in California.

Proposed Accounting and Auditing Regulations

We note that the proposed changes to regulations relating to recordkeeping, accounting, and procedures for annual independent CPA audits are highly technical, and our members are not accountants or auditors. We have consulted with CPAs with very extensive backgrounds in audits

of escrow companies, and they have raised substantial concerns about whether the changes provide clear guidance to CPAs and can ethically be incorporated into audit procedures consistent with national auditing standards. Perhaps most importantly, CPAs have indicated that the changes could materially increase audit costs. CEA would request that the Department modify the proposals such that audit costs are not increased.

More specifically, CEA respectfully opposes language contained in proposed Section 1741.5 (a)(2)(A), which would make licensees responsible to ensuring that audit practitioners perform procedures and prepare reports “in accordance with applicable professional standards.” First, the proposed regulations specifically require the licensee to direct practitioners to report directly to the Commissioner “without any additional notification...from the licensee”, so licensees practically cannot be responsible for the acts of CPAs engaged to perform audits. Second, the language is fundamentally inconsistent with the independence of CPAs so critical to the audit function. Finally, it is completely inappropriate to make licensees responsible for malpractice by independent accountants. This would be tantamount to making clients responsible for attorney malpractice, or patients for medical malpractice. These are independent contractors independently licensed to perform professional services, and should be treated as such.

Prohibited Compensation

As noted above, CEA has for decades been involved in anti-rebate statutes and regulations, at both the state and federal levels. We are aware of RESPA requirements and have great experience in complying with Insurance Code Section 12404. We support the efforts of all escrow regulators in enforcing anti-rebate provisions against escrow providers, however licensed. Respectfully, however, we believe that language in proposed Section 1741.7 on prohibited compensation goes far beyond the Department’s authority in the Financial Code, and would unnecessarily impede legitimate commerce in ways not applicable to other escrow providers.


In terms of authority, we have carefully examined the sections cited by the Department in connection with proposed Section 1741.7. Nothing in Section 17315, relating to the Escrow Agents’ Fidelity Corporation, Section 17400 providing general authority to make rules and adopt forms to carry out the provisions of the Division, or Section 17406, relating to audits and examinations, gives the Department the authority to regulate everyday commerce which might provide volume discounts, let alone social networking and social media activities with other segments of the real estate community. The proposal could even be read to prohibit communications with other real estate professionals on such platforms as LinkedIn.

The purpose of Section 17420 is to prohibit licensees from paying money or other forms of consideration for referring, soliciting, handling or servicing escrow customers or accounts. In concept, this is very similar to the anti-rebate provisions applicable to title entities pursuant to Insurance Code Section 12404. But proposed Section 1741.7, to which Section 17420 is referenced, goes far beyond rebates or kickbacks for the inducement of escrow services, and instead puts the Department squarely in the business of regulating fees.

We would respectfully recommend that the provisions of Section 1741.7 be withdrawn until the industry has the opportunity to evaluate the many issues of pricing implicated in the proposal, potential impacts on commerce, and potential distortions of the competitive escrow market relative to other providers of escrow services.

On behalf of our members throughout California, we appreciate the opportunity to comment on the proposed regulations and would be happy to provide additional information or clarifications upon request.

Sincerely,

DocuSigned by:

Tricia Vagt

President, California Escrow Association