



Escrow Institute of California

Established 1947

February 18, 2021

BY ELECTRONIC SUBMISSION

Sherri.kaufman@DFPI.ca.gov
regulations@dfpi.ca.gov

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 Escrow Institute of California (EIC) is pleased to respond to the California Department of Financial Protection and Innovation (DFPI) proposed changes to the Escrow Law Regulations in CCR Title 10, Chapter 3, Subchapter 9, noticed by the DFPI on 1/4/2021. EIC appreciates the opportunity to review and comment. Following the release of the proposed regulations, EIC convened an ad hoc committee of industry experts including owners of independent escrow companies and expert and seasoned CPA's and attorneys.

EIC respectfully submits the following substantive comments based on the committee's review. The proposed changes are significant and would benefit from further analysis and input from experts and other state and national regulators.

Brief Background

In 2009 the EIC and the DFPI (then known as the Department of Business Oversight) collaborated in passing SB 204 which:

- a) Increased the annual license fee to \$2,800.00;
- b) Changed the DFPI's regulatory audit cycle frequency to not less than every 48 months and;
- c) Added procedures to the annual CPA audit and guidelines for more frequent audits as determined by the DFPI.

In 2013 the DFPI brought the matter of revisions to the annual CPA Audit Procedures to the Escrow Law Advisory Committee based on reports it felt were not satisfactory. A dialogue ensued between the DFPI and CPA professionals as to why the CPA's were unable to meet the DFPI's request within the guidelines of their professional standards of conduct.

In 2015 the DFPI issued a Notice of Proposed Rulemaking regarding the Audit Procedures and obtained, among other things, input from the EIC, expert CPA's and its professional trade associations and other regulators.

In 2017 the DFPI published a Second Notice of Proposed Rulemaking on the CPA Audit Procedures and again obtained input from the EIC and expert CPA's and their professional trade associations and regulators.

The January 2021 Notice of Proposed Rulemaking is an extension and expansion of the CPA Audit Procedures. In addition, it seeks to redefine existing law relating to "kickbacks" by limiting discounting escrow fees for consumers.

Should the DFPI wish to follow its historical pattern seeking the advice and council from subject matter experts, it may be appropriate to immediately establish working groups.

We herein submit the following substantive comments. We, along with CPA's and attorneys, have identified technical comments which at the appropriate time, should be addressed.

EIC's GLOBAL RESPONSE TO PROPOSED REGULATIONS

1. Proposed Regulation: §1741.7 et seq. - Prohibited Compensation

EIC RESPONSE

The Legislature has not authorized the DFPI to regulate escrow fees. Thus, the proposed regulations exceed the statutory authorization (See Financial Code 17420).

In addition, the proposed regulations would diminish protections and opportunities afforded to consumers by unduly regulating fees and the discounts that may be provided to them within the confines of the federal Real Estate Settlement Procedures Act (RESPA) and the related TILA/RESPA Integrated Disclosure (TRID) regulation. As you know, RESPA is a federal anti-kickback statute that prohibits payments for the referral of business in most residential sales situations where there is a mortgage involved. TRID is a federal consumer protection regulation specifically designed to encourage consumers to shop for services and provide guarantees for timely and accurate disclosures. These laws do not set fees that may be charged, or discounts provided. They instead prevent kickbacks for referrals or arrangements where fees are changed at the last minute without suitable cause.

The proposed regulation would also establish an unequal playing field between licensees and exempt escrow practitioners creating a detriment to consumers that contravenes the intent of the legislature regarding kickbacks in SB 133 (a measure directed at the marketing practices of title insurers) as well as the aforementioned RESPA and TRID.

Finally, the proposed regulations run counter to the California Buyer's Choice Act.

The newly prohibited activities are not clearly defined under the current scope in Financial Code Section 17420 and are in conflict with prior guidance.

For these reasons the DFPI may wish to consider withdrawing §1741.7 until the legislature provides clear statutory direction.

2. Proposed Regulation: §1737.3 Records - Records to Be Preserved

EIC RESPONSE

The term “other applicable laws or regulations” in §1737.3(a) is ambiguous and will lead to inconsistent interpretation and does not provide for compliance standards.

The addition, §1737.3(a)(2) could permit the DFPI to look at the front and back of check endorsements which, due to innovations in the banking industry, are not always required.

EIC recommends striking §1737.3(a)(7) because the critical documents needed for an escrow are already defined and without a definitive list and standard for compliance (which is impossible to create due to the varying types of escrows that licensees handle) will lead to inconsistent interpretation.

EIC respectfully requests the DFPI modify the language in 1737.3 (2) to replace the word “printed” with the word “producible”.

3. Proposed Regulation: §1732.2 – Escrow Books

EIC RESPONSE

The terms used in this section are not terms of art in the Accounting Standards Board, California Escrow Law or in case law present. Further, due to the lack of definition of these terms, licensees and their CPAs and attorneys do not use the named forms, nor do they have a general understanding of the required content. This will lead to irregular and inconsistent interpretation and application. One specific example of this is the “Escrow liability controlling account”. It would be appropriate to defer this change unless and until there is agreement upon a definition of the terms, between the DFPI and other state and federal regulators.

4. Proposed Regulation: §1741.5 – Annual Reports

EIC RESPONSE

The expansion and reorganization of procedures required in the “Annual report” as defined in §1741.5(a)(1)(A), including the report of findings and additional documentation, add questionable procedures as delineated below, and will increase costs to licensees and consumers.

The new definition of “dormant escrow balance” in §1741.5(a)(1)(D)(i) is not necessary as the current definition contained in existing regulation §1741.5(H) provides sufficient protection for consumers and the interest of DFPI. We respectfully request this item be stricken.

The title and definition in §1741.5(a)(1)(G) are confusing to licensees and their CPA’s. The EIC recommends working with licensees to formulate a better title and definition to ensure compliance and standardization.

§1741.5(a)(2)(A) violates the CPA’s Ethical Standards and is in direct conflict with §1741.5(a)(2)(B) and therefore the EIC respectfully request that it be stricken.

It is unreasonable to expect that any licensee be liable for the action of an independent CPA as contemplated in §1741.5(a)(2)(B). Further, this section negates the independence of the CPA. Due to the conflict this section creates, the EIC recommends it be struck entirely.

Since the report required in §1741.5(c)(1)(F) is solely for the use of the Commissioner, the EIC recommends it not be made a part of the public record. Further we recommend the public records act language be stricken, given the direction of the California Legislature regarding consumer privacy requirements.

The procedure contained in §1741.5(c)(3)(C)(ii) violates the CPA Professional Standards because it is subjective and lacks clear definition. There is no standard as to what the “characteristics of fraud” are. In an agreed upon procedures agreement, the CPA can only perform procedures and report on the findings. The CPA cannot editorialize on the characteristics of documentation or speculate whether something is likely to contain fraud. Additionally, the proposed regulations conflict with the California Consumer Privacy Act and other state laws.

§1741.5(c)(6)(iv) cannot be performed by the CPA because it is not a procedure. We encourage the Department to work with industry CPA’s to create a procedure.

The procedures described in §1741.5(c)(6)(B)(x) through §1741.5(c)(6)(B)(x)(V) are broad and vague, for example as previously noted, the depository financial institution is responsible for and determines if and how checks are endorsed, and therefore these are not procedures CPA’s can perform.

There is no definition of an “unusual” transaction. The number of checks to be examined is arbitrary and may not make sense in all cases. We do not believe these procedures as written add sufficient value to justify the added time and cost.

§1741.5(d)(2) states the report is solely for the use of the Commissioner, therefore the EIC recommends it not be made a part of the public record. Further we recommend the public records act language be stricken, given the direction of the California Legislature regarding consumer privacy controls.

5. Proposed Regulation: §1741.5.1 – Closing Procedures.

EIC RESPONSE

Industry CPAs have addressed concerns about the procedures as written and about their ability or willingness to comply. We recommend that the DFPI work with the industry CPA’s to refine the procedures in a mutually agreeable way to avoid putting licensees in a position of not being able to obtain a compliance closing report.

These proposed regulations are overly broad and vague as to procedures and definitions. and will affect licensees differently depending on size. It would be appropriate for the proposed regulations to define “unusual activity” and to better define and articulate the procedures. This will avoid differing interpretations.

The requirement that the CPA submit the report directly to the Department before it is reviewed by the licensee limits its ability of the licensee to supervise the work of the CPA to confirm

compliance with the scope and timing requirements. CPA's will be unable to comply with this requirement.

Conclusion

We truly believe everyone would benefit from additional discourse regarding matters at issue. We stand ready to work with the DFPI to achieve that laudable goal and objective.

Sincerely,

DocuSigned by:

BF6DD07EDDF04CC...

PJ Garcia
President, Escrow Institute of California

Cc:
Manual Alvarez, Commissioner, DFPI
Edgar Gill, Senior Deputy Commissioner