

February 19, 2021

BY ELECTRONIC SUBMISSION

regulations@dfpi.ca.gov

Honorable Manuel P. Alvarez
Commissioner of Financial Protection and Innovation
ATTENTION: Sherry Kaufman, and Regulations Coordinator
Department of Financial Protection and Innovation
300 S. Spring Street, Suite 15513
Los Angeles, California 90013

Regarding: Escrow Regulations Docket No.: PRO 13/13

Dear Commissioner Alvarez:

On behalf of Pure Logic Escrow, Inc., which holds an escrow license by the Department of Financial Protection and Innovation (DFPI), I appreciate the opportunity to comment on the proposal to alter the regulations governing the escrow companies licensed by the DFPI.

Some background regarding Pure Logic Escrow (Pure Logic). Since its licensing in 2013, Pure Logic established a unique business model whereby it does not charge sellers an escrow fee. As part of this business model, the buyers' fees are not increased to compensate. Pure Logic provides full escrow services at half the cost to the consumers. Sellers are not charged an escrow fee whether or not they have a broker, and even if they fail to ask about the zero-seller fee offering. All sellers are not charged an escrow fee. This business model provides consumers a choice of selecting an escrow company with a fee structure that fits their budget. Pure Logic's simple fee structure has received a positive welcome by consumers in the industry and has permitted it to expand to seven licensed locations throughout Southern California under the DFPI supervision.

This business model was instituted as management believed escrow agents too often received requests to reduce or discount fees from brokers or are asked to reduce fees to match a competitor's quote. The business model removes the need for promotional schemes or negotiating additional lawful fee reductions to consumers at the request of their representatives. Pure Logic vetted this business model eight years ago through its attorney and was advised by the Department regulating licensees that the Escrow Law does not restrict the fees that an escrow agent may charge for services to the Seller, Buyer, Lender or Borrower. The Department's own website has for many years stated unequivocally that:

13. ARE THE FEES ESCROW AGENTS CHARGE FOR THEIR SERVICES REGULATED?

The Escrow Law does not restrict the fees that escrow agents may charge for services. The amounts escrow agents charge for their services vary depending on the location of the escrow agent, type of transaction and the competition in the area. The escrow agent is required to disclose all fees on the closing statement that is prepared after the transaction is completed. It is recommended that you request that the escrow agent provide you with a fee schedule that shows the charges for their services.¹

We are mindful of Financial Code Section 17420, and its restrictions on payment of referral fees. This business model directly avoids any violation of Section 17420 by only benefiting the consumer on transactions. A fee waiver is never provided based on the consumer's representation by a Broker, nor is a discount ever provided to any referring person.

Concerns with Section 1741.7 - Prohibited Compensation

Pure Logic believes the Department should withdraw proposed provision in 1741.7 and address its concerns underlying the provision in a separate proposal and rulemaking within its authority. If it seeks to restrict the amount of fees charged by its licensees it should seek additional authority from the legislature by seeking to amend the Financial Code itself.

In addressing the context of Section 1741.7 and our objections to the proposal, we will address specific concerns we believe should affect the adoption of these proposed changes or result in the withdraw of Section 1741.7 for reconsideration in a future rulemaking after additional legal and policy review.

In general, Section 1741.7 fails to sufficiently identify its connection to Financial Code Section 17420 restriction on the payment of referral fees. Section 1741.7 appear to establish new law by rulemaking certain finite acts listed as now prohibited compensation. These findings of prohibited compensation depart from the individualized factual analysis the Department has engaged in through its Bulletins on these subjects or through its active enforcement of Financial Code Section 17420. Section 1741.7 departs from years of guidance from the Department that the prohibitions in Financial Code 17420 are limited to direct or indirect compensation for referring, soliciting, handling or servicing escrow business and not a wholesale prohibition on activities. The Escrow Law and Commissioner's authority never before extended to set fees.

In Section 1741.7 (a)(6) the Commissioner proposes a rule that "offering free escrow service to one or more parties to the escrow" is a violation and prohibited compensation. This rule appears to be directly targeted at Pure Logic and a small minority of similar escrow licensees who have established a business model that provide escrow services for a reduced fee. The Department

¹ <https://dfpi.ca.gov/escrow-law-frequently-asked-questions/>

should not through rulemaking react to pressure from other Escrow licensees faced with lawful competition at lower rates to the consumer by setting rate to prohibit competition.

Further Section 1741.7 (a)(6) demonstrates no nexus to Financial Code Section 17420 and why a “free escrow service” to a direct principal of the transaction violates the law. Both RESPA Rule 8 and Section 17420 make it unlawful to provide such services for free if given in conjunction with an actual or implied referral fee to a broker or agent, but they do not prohibit discounts, reduced fees, or free services if they are provided to the consumer directly. RESPA Rule 8, is not a total prohibition statute and even identifies permitted conduct. Section 1741.7 fails to make such distinctions and is a de facto prohibition of all conduct.

Section 1741.7 (a)(7) (A-E) is also de facto rate/fee setting rule which seeks to control competition. Either intentionally or unintentionally, the sub-sections set forth arbitrary conditions to set rates for escrow services that are dependent on the terms of contracts. The Department overlooks the right to freely negotiate contracts and escrow services is a three person agreement typically Buyer, Seller and Escrow Agent where the terms, including price, for performing escrow services.

This rule, as proposed, appears to borrow concepts from the legislative enactment in the Insurance Code but fails to seek the assistance from the legislature to enact new laws here. Instead, sub-section (7)(A) of Section 1741.7 (a) lists finite rules for what the Department finds an acceptable condition for a discount. These stated conditions are without a statement of factual findings supporting such conditions and are contrary to decades of guidance from the Department and is contrary to California case precedent. We have understood, as noted in Sub-section (7)(C), that any discount cannot contravene the allocation for payment of escrow fee agreed upon by the parties. However, Sub-sections (7) (A-B) limits discounts to both principals or require both principals to mutually agree on a change in the escrow fee, which is not supported in any Escrow Law, statutes or case authority. These Sub-sections unfairly restrict the open negotiation of escrow fees, stifle competition, and will result in standard fees across the industry at higher rates by consumers.

Particularly troubling is Sub-section (7)(D) of Section 1741.7 (a) which attempts to equate the size of a fee discount or the escrow fee charged with the independence of the escrow agent in the transaction. This was considered and rejected by the Legislator when it enacted Financial Code Section 17006, with persons exempt from the Escrow Law regulatory scheme. Specifically, Section 17006 (a) excluded (1) banks, (2) persons licensed in California to practice law “who has a bona fide client relationship with a principal”; (3) Title companies in the business of issuing a policy of title insurance; and (4) any broker licensed by the Real Estate Commissioner while performing acts where the broker is an agent to a party to the transaction. In three of four persons, the Legislature found exempt from the Escrow Laws, are persons acting in a role that is not independent. Attorneys can only process escrow when they have a client relationship with a principal. The attorney’s fiduciary duties to his client directly conflicts with his independence as

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an escrow agent. Similarly, a Title Company is not independent when it serves as escrow agent, offering low escrow fees, while also collecting a premium for issuing a policy of title insurance. Further, a Broker is not an independent escrow agent when acting as the Broker to one principal.

On a practical level, Sub-section (7)(D), is fatally uncertain to licensees and ultimately not enforceable by the Department. The sub-section is ambiguous as it fails to establish what amount of a discount is large enough to affect the independence of the escrow agent. One may contend that an escrow agent is more independent when free escrow services are given. Similarly, is an attorney less independent when services are pro-bono? However, perhaps the greater the fee charged for escrow services the more independent the escrow agent can be. This is an unworkable standard, and should be withdrawn.

Conclusion

We believe the Department may be exceeding its authority in proposing section 1741.7. This proposed regulation is too broad, is ambiguous, will be difficult to enforce and will harm consumers. We ask that the Department withdraw Section 1741.7 and consult with industry professionals to address the concerns the provisions sought to address.

Thank you for the opportunity to comment and during a public hearing scheduled.

Sincerely,

Jamie Brennan
President

Cc:
Sherri Kaufman, Senior Counsel and Regulatory Coordinator