TO: All State Credit Unions

FROM: Joseph M. Vincent
Director of Regulatory & Legal Affairs

RE: Deposit-Taking – Interest-on-Real-Estate Trust Accounts (IRETAs)

DATE: June 16, 2017

This Interpretive Letter is being issued by Joseph M. Vincent, Director of Regulatory & Legal Affairs for the Washington State Department of Financial Institutions (“Department”), acting under express authority from Linda K. Jekel, the Department’s Director of Credit Unions.

1.0 BACKGROUND

An interest-on-real estate trust account (“IRETA”) is a specialized interest earning account used for the deposits of pooled client funds by real estate professionals. It is very similar in both principle and procedure to the more commonly known interest-on-lawyer’s trust account (“IOLTA”). Several Washington state-chartered banks offer to maintain not only IOLTA funds but also IRETA funds.1

Under Washington State law, every real estate firm that keeps separate real estate trust fund accounts must keep those accounts in a recognized Washington state depository. A real estate firm must maintain an adequate amount of funds in the trust fund accounts to facilitate the opening of the trust fund accounts or to prevent the closing of the trust fund accounts.2 If a real estate broker receives or maintains earnest money or client funds for deposit, the real estate firm must maintain a pooled interest-bearing trust account for deposit of those client funds.3 This does not, however, include property management trust accounts.4

Such a pooled interest-bearing trust account, created by a real estate broker for receiving or maintaining earnest money or client funds on deposit with a financial institution, is known as an IRETA.

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1 See for example, Coastal Community Bank’s website: https://www.coastalbank.com/business/checking/iolta-ireta.html.
2 RCW 18.85.285(4).
3 RCW 18.85.285(8)(a).
4 Id.
2.0 ISSUES

1. Is a Washington State-chartered credit union (“State Credit Union”) authorized to maintain IRETA accounts?

2. If so, what must a State Credit Union do with the interest earned on IRETAs it administers, and what other reporting requirements does the State Credit Union have in this regard?

3.0 SHORT ANSWER

A State Credit Union is authorized under both federal and state law to keep and maintain IRETAs for Washington State real estate brokers. The requirements of a State Credit Union in its administering of IRETA accounts are as set forth in the analysis below.

To the extent that the same or similar principles and procedures apply in a state other than Washington in which a State Credit Union may have a deposit-taking branch, a State Credit Union may maintain an IRETA account of a real estate broker licensed in that other state.

4.0 ANALYSIS

4.1 Authority under the Federal Credit Union Act. Federal Credit Union Act (“FCUA”) amendments in 2014 provided for enhanced, pass-through share insurance for IOLTAs and other similar escrows. The FCUA declares, in relevant part, as follows:

(5) Coverage for interest on lawyers trust accounts (IOLTA) and other similar escrow accounts
(A) Pass-through insurance
   The Administration shall provide pass-through share insurance for the deposits or shares of any interest on lawyers trust account (IOLTA) or other similar escrow accounts.
(B) Treatment of IOLTAs
   (i) Treatment as escrow accounts
   For share insurance purposes, IOLTAs are treated as escrow accounts.
   (ii) Treatment as member accounts
   IOLTAs and other similar escrow accounts are considered member accounts for purposes of paragraph (1), if the attorney administering the IOLTA or the escrow agent administering the escrow account is a member of the insured credit union in which the funds are held.
(C) Definitions. For purposes of this paragraph:
   (i) Interest on lawyers trust account
   The terms “interest on lawyers trust account” and “IOLTA” mean a system in which lawyers place certain client funds in interest-bearing or dividend-bearing accounts, with the interest or

dividends then used to fund programs such as legal service organizations who provide services to clients in need.

(ii) Pass-through share insurance

The term “pass-through share insurance” means, with respect to IOLTAs and other similar escrow accounts, insurance coverage based on the interest of each person on whose behalf funds are held in such accounts by the attorney administering the IOLTA or the escrow agent administering a similar escrow account, in accordance with regulations issued by the Administration.

(D) Rule of construction

No provision of this paragraph shall be construed as authorizing an insured credit union to accept the deposits of an IOLTA or similar escrow account in an amount greater than such credit union is authorized to accept under any other provision of Federal or State law.6

[Emphasis added.]

The phrase, “and other similar escrow accounts,” is somewhat unartful. IRETAs are not escrow accounts per se. They only become so when the funds (e.g., earnest money) are transferred to an escrow agent for closing. They are, however, trust funds. An escrow is a fiduciary (trust) relationship but is typically thought of as a more specialized one.

The FDIC regulations are much broader for banks and do not even mention IOLTA by name. To be insured by the FDIC, an agent or nominee account like an IOLTA must expressly disclose, by way of specific reference, the existence of any fiduciary relationship such as an agent or nominee pursuant to which funds are deposited into a bank account and on which a claim for deposit insurance coverage is based. The FDIC has stated that such an account, including an IOLTA, must disclose that the funds are held by the nominal account holder on the behalf of others.7

However, to be fair to credit unions, we ought to consider that Congress’ use of language meant that they would likely perceive an IRETA to be an “escrow account” for pass-through deposit insurance purposes, otherwise why use the phrase, “and other similar escrow accounts.” IRETAs, in effect, perform the same or a similar function for real estate brokers that the IOLTA does for attorneys – they are trust funds and are denominated as such.

4.2 Authority under the 2016 NCUA Rule. The National Credit Union Administration (“NCUA”), in reliance upon the 2014 FCUA amendment, adopted a rule covering IOLTA accounts “and other similar escrow accounts,” effective January 27, 2016, which added a section to Subpart A of Part 745 of Title 12 of the Code of Federal Regulations (12 C.F.R. Part 745). This new section of Part 745 reads in relevant part, as follows:

§ 745.14 Interest on lawyers trust accounts and other similar escrow accounts.

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6 Id.

(a)(1) **Pass-through share insurance.** The deposits or shares of any interest on lawyers trust account (IOLTA) or other similar escrow account in an insured credit union are insured on a “pass-through” basis, in the amount of up to the SMSIA\(^8\) for each client and principal on whose behalf funds are held in such accounts by either the attorney administering the IOLTA or the escrow agent administering a similar escrow account, in accordance with the other share insurance provisions of this part.  
(2) **Pass-through coverage will only be available if the recordkeeping requirements of §745.2(c)(1) of this part and the relationship disclosure requirements of §745.2(c)(2) of this part are satisfied.** . . .

(b) **Membership requirements and treatment of IOLTAs.** For share insurance purposes, IOLTAs are treated as escrow accounts. IOLTAs and other similar escrow accounts are considered member accounts and eligible for pass-through share insurance if the attorney administering the IOLTA or the escrow agent administering the escrow account is a member of the insured credit union in which the funds are held. In this circumstance, the membership status of the clients or the principals is irrelevant.

(c) **Definitions.** For purposes of this section:

(iii) Other similar escrow account means an account where a licensed professional or other individual serving in a fiduciary capacity holds funds for the benefit of a client or principal as part of a transaction or business relationship. Examples of such accounts include, but are not limited to, real estate escrow accounts and prepaid funeral accounts.

(iii) **Pass-through share insurance means, with respect to IOLTAs and other similar escrow accounts, insurance coverage based on the interest of each person on whose behalf funds are held in such accounts by the attorney administering the IOLTA or the escrow agent administering a similar escrow account.** . . .\(^9\)

Based upon the afore-mentioned NCUA rule, it is fairly clear that the NCUA has interpreted its authority from Congress to permit pass-through deposit insurance to “real estate escrow accounts.”\(^10\) What is not clear is what the NCUA means by a “real estate escrow account.” By using that example only, does NCUA mean the escrow account of a title company or real estate escrow agent? Or does the NCUA also mean a real estate broker holding earnest money?\(^11\) Accordingly, the Division of Credit Unions cannot rely upon the NCUA Rule alone as

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\(^8\) SMSIA is the standard maximum share insurance amount. See 12 C.F.R. 745.1(e).


\(^10\) 12 C.F.R. § 745.14(c)(ii).

\(^11\) “Other similar escrow account,” as defined in 12 C.F.R. §745.14(c)(2), “ means an account where a licensed professional or other individual serving in a fiduciary capacity holds funds for the benefit of a client or principal as part of a transaction or business relationship.” Notwithstanding the lack of clarity with respect to “real estate escrow agent” as its example, the Division of Credit Unions is confident in its
dispositive of whether a State Credit Union may administer an IRETA for a real estate broker depositing earnest money.

4.3 **An IRETA as an Incidental Power of a State Credit Union.** Notwithstanding the NCUA’s lack of clarity as set forth in Subsection 4.2 above, the Director of Credit Unions, in combination with an understanding of Congress’ intent as discussed above in Subsection 4.1, does have the authority to declare the administration of an IRETA as an incidental power of a State Credit Union pursuant to the Washington Credit Union Act (“WCUA”), provided that this activity is “necessary or convenient to enable [a State Credit Union] to conduct the business of a credit union.”12 Moreover, the statutory purpose of the Director of Credit Unions includes “protect[ing] . . . the interests of the general public, and . . . ensur[ing] that credit unions remain viable and competitive in this state.”13

Accordingly, to that end, the Director of Regulatory & Legal Affairs, acting under the express authority of the Director of Credit Unions, does hereby determine that the administering of IRETA accounts by a State Credit Union, consistent with the requirements of this Interpretive Letter, is a permissible incidental power of a State Credit Union under the WCUA.

4.4 **Director’s Requirements for Administering IRETAs – NCUA Rules.** Even though the NCUA Rule was not completely clear as to the meaning of “other similar escrow accounts,” the NCUA Rule is sufficiently clear as to the following safety-and-soundness requirements concerning the administration of an IRETA. These include:

- Maintaining the NCUA’s SMSIA limit for each client and principal on whose behalf funds are held in such accounts by a real estate broker;14
- Following the NCUA’s recordkeeping requirements for insurance of accounts;15 and
- Complying with the NCUA’s relationship disclosure requirements.16

A State Credit Union administering an IRETA must comply with all three of the above.

4.5 **Director’s Requirements for Administering IRETAs – Washington Real Estate Brokerage Law and Rule Generally.** Among the trust account requirements and exemptions for real estate brokerage firms under Washington State law are the following statutory obligations:

- A real estate brokerage firm must maintain a separate real estate trust fund account or accounts in a Washington State depositary;17

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14 12 C.F.R. §745.14(a)(1).
15 12 C.F.R. §§745.2(c)(1) and 745.14(a)(2).
16 12 C.F.R. §§745.2(c)(2) and 745.14(a)(2).
17 RCW 18.85.285(4).
• It must maintain enough in such trust accounts to facilitate their opening and prevent their closing;\(^{18}\)
• It is not required to maintain a trust fund account for transactions concerning a purchase and sale agreement that instructs the broker to deliver the earnest money check directly to a named closing agent\(^{19}\) or to the seller;\(^ {20}\)
• It must deposit trust funds with the State Credit Union the next banking day following their receipt unless the purchase and sale agreement has a provision for deferred deposit;\(^ {21}\)
• Earnest money or client funds for deposit must be placed in a pooled interest-bearing account known commonly as an IRETA account;\(^ {22}\)
• Property management trust accounts are to be treated differently than IRETA accounts involving earnest money or client funds on deposit;\(^ {23}\)
• After a State Credit Union nets out a reasonable and appropriate service charge or fee, interest on the IRETA account is to be paid to the State Treasurer for the Washington Housing Trust Fund\(^ {24}\) and Real Estate Education Program Account;\(^ {25}\)\(^ {26}\)
• The firm or designated broker is not required to notify the client of the intended use of the funds;\(^ {27}\)
• The real estate broker must direct a State Credit Union to:
  ○ Remit the interest on IRETA accounts, net of any reasonable and appropriate service charges or fees, on the average monthly balance in the account, or as otherwise computed in accordance with a State Credit Union’s standard accounting practice, at least quarterly, to the \textit{State Treasurer} for deposit in the Housing Trust Fund and the Real Estate Education Program Account;\(^ {28}\)\(^ {29}\) and
  ○ Transmit to the \textit{Department of Commerce} a statement showing the name of the person(s) on behalf of whom trust deposits were made, the rate of interest applied, and the amount of service charges deducted, if any, and the account balance(s) of the period in which the report is made, with a copy of the statement to be transmitted to the real estate broker;\(^ {30}\) and
• The Department of Commerce then forwards a copy of these reports to the \textit{Department of Licensing} to aid in enforcement.\(^ {30}\)

For safety-and-soundness purposes, any State Credit Union administering an IRETA program must be mindful of the requirements of its members who are subject to provisions set

\(^{18}\) Id.
\(^{19}\) This kind of account, maintained by a real estate escrow agent and deposited by her with a State Credit Union, would be treated as an IOLTA account rather than an IRETA account.
\(^{20}\) RCW 18.85.285(6).
\(^{21}\) RCW 18.85.285(7).
\(^{22}\) RCW 18.85.285(8)(a).
\(^{23}\) Id.
\(^{24}\) RCW 43.185.030 declares: “There is hereby created in the state treasury an account to be known as the \textit{Washington housing trust fund}. The housing trust fund shall include revenue from the sources established by this chapter, appropriations by the legislature, private contributions, repayment of loans, and all other sources. . . .” [Emphasis added.]
\(^{25}\) RCW 18.85.321 declares: “The \textit{real estate education program account} is created in the custody of the state treasurer. All moneys received for credit to this account pursuant to RCW 18.85.311 and all moneys derived from fines imposed under this chapter shall be deposited into the account. . . .” [Emphasis added.]
\(^{26}\) RCW 18.85.285(8)(b).
\(^{27}\) Id.
\(^{28}\) RCW 18.85.285(10)(a).
\(^{29}\) Id.
\(^{30}\) RCW 18.85.285(11).
forth above. Moreover, nothing in the requirements set forth above relieves a real estate broker or her firm of any obligation with respect to safekeeping of clients’ funds.\(^{31}\) See complete text of statute, Appendix A.

In addition, a State Credit Union administering an IRETA program must comply with the following trust account procedures of the Department of Licensing under the Washington Administrative Code (“WAC”), as applicable:

- The general procedures for administration of funds held in trust, as set forth in WAC 308-124E-105 and reproduced in Appendix B of this Interpretive Letter; and
- The specific procedures for administration of funds held in trust by real estate sales professionals, as set forth in WAC 308-124E-110 and reproduced in Appendix C of this Interpretive Letter.

### 4.6 Director’s Special Requirements Related to “Property Management” Funds Held in Trust

Interest on IRETA accounts involving a real estate broker’s property management for an owner is entitled to be remitted to the landlord-owner.\(^{32}\) In other words, the remittance rules applicable to real-estate earnest money and broker client funds on deposit, as set forth above in Subsection 4.5, do not apply to IRETA accounts for property managers. However, a State Credit Union should become familiar with the Department of Licensing’s WAC provisions applicable to trust funds held by property managers (typically landlord’s security and damage deposits). See the complete provisions at Appendix D.

One WAC provision of particular note in regard to property managers is the restriction that declares that a preauthorization of disbursements or deductions by a State Credit Union for recurring expenses, such as mortgage payments on behalf of the owner, is not permitted if the account contains tenant security deposits or funds belonging to more than one client (i.e., a pooled account).\(^{33}\)

So it has been asked by one or more State Credit Unions what responsibility (if at all) a State Credit Union has to make sure such prohibited disbursements and deductions for recurring expenses do not occur. The answer is to be found in the Washington Financial Institution Individual Account Deposit Act, which provides that any financial institution as defined in that Act, including a State Credit Union, has immunity from liability, as follows:

In making payments of funds deposited in an account, a financial institution may rely conclusively and entirely upon the form of the account and the terms of the contract of deposit at the time the payments are made. A financial institution is not required to inquire as to either the source or the ownership of any funds received for deposit to an account, or to the proposed application of any payments made from an account. Unless a financial institution has actual knowledge of the existence of dispute between depositors, beneficiaries, or other persons claiming an

\(^{31}\) RCW 18.85.285(12)(a).

\(^{32}\) WAC 308-124E-115(1)(a)-(b).

\(^{33}\) WAC 308-124E-115(3).
interest in funds deposited in an account, all payments made by a financial institution from an account at the request of any depositor to the account and/or the agent of any depositor to the account in accordance with this section and RCW 30A.22.140, 30A.22.150, 30A.22.160, 30A.22.170, 30A.22.180, 30A.22.190, 30A.22.200, and 30A.22.220 shall constitute a complete release and discharge of the financial institution from all claims for the amounts so paid regardless of whether or not the payment is consistent with the actual ownership of the funds deposited in an account by a depositor and/or the actual ownership of the funds as between depositors and/or the beneficiaries of P.O.D. and trust accounts, and/or their heirs, successors, personal representatives, and assigns.\(^{34}\)

However, notwithstanding the above-cited immunity provision, a State Credit Union should exercise initial and ongoing due diligence with a property manager who takes security and damage deposits from more than one landlord-client in a single IRETA account.

### 4.7 IRS 1099 Reporting for Interest on IRETA Accounts.

As of this writing, the Division of Credit Unions knows of no revenue ruling with respect to IRETA accounts where interest is payable to state government-mandated funds in which clients, real estate brokers, and financial institutions have no choice but to comply.

There is, however, a plethora of law and rule on the subject of IOLTA accounts in this regard. With respect to IOLTA accounts, the Internal Revenue Service (“IRS”) ruled in 1981 that interest earned on clients' nominal and short-term advances of a lawyer’s clients and paid over to a charitable foundation is not includible in the gross incomes of the clients,\(^{35}\) which would therefore preclude having to issue IRS 1099 income statements. This was amplified later by an IRS Revenue Ruling with respect to a state-mandated Lawyer Trust Account Fund to which interest would be paid,\(^{36}\) in which the IRS held that that because neither the clients nor the lawyers have control over, or right to, interest on pooled accounts paid over to the Fund, the interest paid over to the Fund is not taxable to either the clients or lawyers. Moreover, the IRS has acknowledged that a client whose funds are placed in an IOLTA account cannot elect or veto participation. It is the law, and they have no choice.

Now, in *Phillips v. Washington Legal Foundation*,\(^{37}\) the Supreme Court of the United States did hold that interest earned on client funds held in IOLTA accounts is the “private property” of the client for purposes of the Takings Clause (U.S. Const. amend. V). However, the Court left for consideration on remand the question whether IOLTA funds have been “taken” by the state, as well as the amount of “just compensation,” if any, due to the clients. Thus, the Court did not hold that the client had any control over, or right to, interest on the IOLTA trust account.

Based on the above, it has been the position of the IRS that interest earned on client's funds deposited in an IOLTA account and paid to a State-mandated fund is not includible in the

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\(^{34}\) RCW 30A.22.120.

\(^{35}\) IRS Rev. Rul. 81-209.


income of client or the law firm. Therefore, a financial institution is not required under the Internal Revenue Code\textsuperscript{38} to report interest paid to such a State-mandated fund on an information return, because the Foundation is an organization exempt from tax\textsuperscript{39} and is thus an exempt recipient.\textsuperscript{40}

In the case of IRETAs, we have two scenarios as discussed above. With IRETAs maintained by property managers who take trust deposits for security and damage, these are payable or recognized by the landlord-owner. Therefore, in this first instance, IRS 1099s would be required. However, in the case of IRETAs in which interest is required by state law to be paid to the State-mandated Housing Trust Fund and the Real Estate Education Program Account, it would appear, consistent with the Revenue Rulings and Release by the IRS with respect to IOLTA accounts that the same determination by the IRS would hold true for these types of IRETA accounts, i.e., where a real estate broker puts earnest money or client funds on deposit and in which interest is required to be remitted to Washington State’s Housing Trust Fund and the Real Estate Education Program Account.

This reasoning notwithstanding, a State Credit Union is advised to seek a tax opinion from independent legal counsel in order to be assured that this is or would be the IRS position.

4.8 Trust Fund Requirements of Other States Applicable to IRETA Accounts. IRETA accounts are common in other states, and the requirements of other state laws with respect to real estate broker trust funds are, in the preliminary view of the Division of Credit Unions, either the same or similar as those in Washington State. Therefore, to the extent that the same or similar principles and procedures apply in a state other than Washington in which a State Credit Union may have a deposit-taking branch, a State Credit Union may maintain an IRETA account of a real estate broker licensed in that other state, subject to any and all trust fund requirements of that state as they may diverge from those in Washington State.

5.0 Conclusion

This Interpretive Letter is applicable to all State Credit Unions. If you have any questions, please do not hesitate to contact Linda Jekel, Director of Credit Unions, at linda.jekel@dfi.wa.gov, or (360) 902-8778.

\textsuperscript{38} 26 U.S.C §6049.
\textsuperscript{39} 26 U.S.C. §501(a).
\textsuperscript{40} See IRS Release, PLR-110527-98 (March 5, 1999), \url{https://www.irs.gov/pub/irs-wd/9909032.pdf}.
APPENDIX A

RCW 18.85.285 Transactions and recordkeeping—Trust accounts—Requirements.

(1) Brokers and managing brokers must submit complete copies of their transactions to their firm. The designated broker shall keep adequate records of all real estate transactions handled by or through the firm or firms to which the designated broker is registered. The records shall include, but are not limited to, a copy of the purchase and sale agreement, earnest money receipt, and an itemization of the receipts and disbursements with each transaction. These records and all other records specified by the director by rule are open to inspection by the director or the director's authorized representatives.

(2) If any licensee exercises control over real estate transaction funds, those funds are considered trust funds.

(3) Every real estate licensee shall deliver or cause to be delivered to all parties signing the same, within a reasonable time after signing, purchase and sale agreements, listing agreements, and all other like or similar instruments signed by the parties.

(4) Every real estate firm that keeps separate real estate trust fund accounts must keep the accounts in a recognized Washington state depository. A real estate firm must maintain an adequate amount of funds in the trust fund accounts to facilitate the opening of the trust fund accounts or to prevent the closing of the trust fund accounts.

(5) All licensees shall keep separate and apart and physically segregated from the licensees' own funds, all funds or moneys including advance fees of clients that are being held by the licensees pending the closing of a real estate sale or transaction, or that have been collected for the clients and are being held for disbursement for or to the clients.

(6) A firm is not required to maintain a trust fund account for transactions concerning a purchase and sale agreement that instructs the broker to deliver the earnest money check directly to a named closing agent or to the seller.

(7) Brokers must deposit all funds into their firm's trust bank account the next banking day following receipt of the funds unless the purchase and sale agreement provides for deferred deposit or delivery. In that event, the broker must promptly deposit or defer funds in accordance with the terms of the purchase and sale agreement.

(8)(a) If a real estate broker receives or maintains earnest money or client funds for deposit, the real estate firm shall maintain a pooled interest-bearing trust account for deposit of client funds, with the exception of property management trust accounts.

(b) The interest accruing on this account, net of any reasonable and appropriate financial institution service charges or fees, shall be paid to the state treasurer for deposit in the Washington housing trust fund created in RCW 43.185.030 and the real estate education program account created in RCW 18.85.321. Appropriate service charges or fees are those charges made by financial institutions on other demand deposit or "now" accounts. The firm or designated broker is not required to notify the client of the intended use of the funds.

(c) The department shall adopt rules that will serve as guidelines in the choice of an account specified in this subsection.

(9) If trust funds are claimed by more than one party, the designated broker or designated broker's delegate must promptly provide written notification to all contracting parties to a real estate transaction of the intent of the designated broker or designated broker's delegate to disburse client funds. The notification must include the names and addresses of all parties to the contract, the amount of money held and to whom it will be disbursed, and the date of disbursement that must occur no later than thirty consecutive days after the notification date.

(10) For an account created under subsection (8) of this section, the designated or managing broker shall direct the depository institution to:

(a) Remit interest or dividends, net of any reasonable and appropriate service charges or fees, on the average monthly balance in the account, or as otherwise computed in accordance with an institution's standard accounting practice, at least quarterly, to the state treasurer for deposit in the housing trust fund created by RCW 43.185.030 and the real estate education program account created in RCW 18.85.321; and

(b) Transmit to the [Department of Commerce] a statement showing the name of the person or entity for whom the remittance is spent, the rate of interest applied, and the amount of service charges deducted, if any, and the account balance(s) of the period in which the report is made, with a copy of the statement to be transmitted to the depositing person or firm.

(11) The [Department of Commerce] shall forward a copy of the reports required by subsection (10) of this section to the department to aid in the enforcement of the requirements of this section consistent with the normal enforcement and auditing practices of the department.

(12)(a) This section does not relieve any real estate broker, managing broker, or firm of any obligation with respect to the safekeeping of clients' funds.
(b) Any violation by real estate brokers, managing brokers, or firms of any of the provisions of this section, RCW 18.85.361, or chapter 18.235 RCW is grounds for disciplinary action against the licenses issued to the brokers, managing brokers, or firms.
APPENDIX B

WAC 308-124E-105 Administration of funds held in trust—General procedures.

Any real estate broker who receives funds or moneys from any principal or any party to a real estate or business opportunity transaction, property management agreement, contract/mortgage collection agreement, or advance fees, shall hold the funds or moneys in trust for the purposes of the brokerage service contract or transaction, and shall not utilize such funds or moneys for the benefit of the broker, managing broker, real estate firm or any person not entitled to such benefit. Designated brokers are responsible for ensuring their affiliated licensees safeguard client funds by following these rules. Funds or moneys received in trust shall be deposited in a bank, savings association, or credit union insured by the Federal Deposit Insurance Corporation or the share insurance fund of the National Credit Union Administration, or any successor federal deposit insurer. The financial institution must be able to accept service in Washington state. The designated broker is responsible for the administration of trust funds and accounts to include, but not be limited to:

- Depositing;
- Holding;
- Disbursing;
- Receipting;
- Posting;
- Recording;
- Accounting to principals;
- Notifying principals and cooperating licensees of material facts; and
- Reconciling and properly setting up a trust account. The designated broker is responsible for handling trust funds as provided herein.

(1) Bank accounts shall be designated as trust accounts in the firm name or assumed name as licensed.

(2) Interest credited to a client's account must be recorded as a liability on client ledger. Interest assigned or credited by written assignment agreement to the firm may not be maintained in the trust account. The designated broker is responsible for making arrangements with the financial institution to credit this interest to the general account of the firm.

(3) The designated broker shall establish and maintain a system of records and procedures approved by the real estate program that provides for an audit trail accounting of all funds received and disbursed. All funds must be identified to the account of each individual client.

(4) Alternative systems of records or procedures proposed by a designated broker shall be approved in advance in writing by the real estate program.

(5) The designated broker shall be responsible for deposits, disbursements, or transfers of clients' funds received and held in trust.

(6) All funds or moneys received for any reason pertaining to the sale, renting, leasing, optioning of real estate or business opportunities, contract or mortgage collections or advance fees shall be deposited in the firm's real estate trust bank account not later than the next banking day following receipt thereof; except:

(a) Cash must be deposited in the firm's trust account not later than the next banking day;
(b) Checks received as earnest money deposits when the earnest money agreement states that a check is to be held for a specified length of time or until the occurrence of a specific event; and
(c) For purposes of this section, Saturday, Sunday, or other legal holidays as defined in RCW 1.16.050 shall not be considered a banking day.

(7) All checks, funds or moneys received shall be identified by the date received and by the amount, source and purpose on either a cash receipts journal or duplicate receipt retained as a permanent record.

(8) All deposits to the trust bank account shall be identified by the source of funds and transaction to which it applies.

(9) An individual client's ledger sheet shall be established and maintained for each client for whom funds are received in trust, which shows all receipts and disbursements. The firm will maintain the minimum amount required by the financial institution in the trust account to prevent the trust account from being closed. A ledger sheet identified as "opening account" will be required for funds that are used to open the account or to keep the trust account from being closed. The debit entries must show the date of deposit, amount of deposit, and item covered including, but not limited to "earnest money deposit," "down payment," "rent," "damage deposit," "rent deposit," "interest," or "advance fee." The debit entries must show the date of the check, check number, amount of the check, name of payee and item covered. The "item covered" entry may indicate a code number per chart of accounts, or may be documented by entry in a cash receipts journal, cash disbursements journal, or check voucher.
(10) The reconciled real estate trust bank account balance must be equal at all times to the outstanding trust liability to clients and the funds in the "open account" ledger. The balance shown in the check register or bank control account must equal the total liability to clients and the "open account" ledger.

(11) The designated broker shall be responsible for preparation of a monthly trial balance of the client's ledger, reconciling the ledger with both the trust account bank statement and the trust account check register or bank control account. The checkbook balance, the bank reconciliation and the client ledgers (including the "open account" ledger) must be in agreement at all times. A trial balance is a listing of all client ledgers, including the "open account" ledger, showing the owner name or control number, date of last entry to the ledger and the ledger balance.

(12) All disbursements of trust funds shall be made by check, or electronic transfer, drawn on the real estate trust bank account and identified thereon to a specific real estate or business opportunity transaction, or collection/management agreement. The number of each check, amount, date, payee, items covered and the specific client's ledger sheet debited must be shown on the check stub or check register and all data must agree exactly with the check as written. No check numbers on any single trust account can be duplicated.

(a) No disbursement from the trust account shall be made based upon wire transfer receipts until the deposit has been verified.

(b) The designated broker must provide a follow-up "hard-copy" debit memo when funds are disbursed via wire transfer.

(c) The designated broker shall retain in the transaction file a copy of instructions signed by the owner of funds to be wire-transferred which identifies the receiving entity and account number.

(13) Voided checks written on the trust bank account shall be permanently defaced and shall be retained.

(14) Commissions owed to another firm may be paid from the real estate trust bank account. Those commissions shall be paid promptly upon receipt of funds. Commissions shared with another firm are a reduction of the gross commissions received.

(15) No deposits to the real estate trust bank account shall be made of funds:

(a) That belong to the designated broker or the real estate firm, except that a designated broker may deposit a minimal amount to open the trust bank account or maintain a minimal amount to keep the account from being closed; or

(b) That do not pertain to a client's real estate or business opportunity sales transaction or are not received in connection with a client's rental, contract or mortgage collection account.

(16) No disbursements from the real estate trust bank account shall be made:

(a) For items not pertaining to a specific real estate or business opportunity transaction or a rental, contract or mortgage collection account;

(b) pertaining to a specific real estate or business opportunity transaction or a rental, contract or mortgage collection account in excess of the actual amount held in the real estate trust bank account in connection with that transaction or collection account;

(c) In payment of a commission owed to any person licensed to the firm or in payment of any business expense of the firm. Payment of commissions to persons licensed to the firm or of any business expense of the designated broker or firm shall be paid from the regular business bank account of the firm.

(d) For bank charges of any nature, including bank services, checks or other items, except as specified in WAC 308-124E-110 (1)(a) and (d). Bank charges are business overhead expenses of the real estate firm. Arrangements must be made with the bank to have any such charges applicable to the real estate trust bank account charged to the regular business bank account, or to provide a separate monthly statement of bank charges so that they may be paid from the firm's business bank account.

(17) The provisions of this chapter are applicable to manual or computerized accounting systems. For clarity, the following is addressed for computer systems:

(a) The system must provide for a capability to back up all data files.

(b) Receipt, check or disbursement registers or journals, bank reconciliations, and monthly trial balances will be maintained and available for immediate retrieval or printing upon demand of the department.

(c) The designated broker will maintain a dated source document file or index file to support any changes to existing accounting records.
APPENDIX C

WAC 308-124E-110
Administration of funds held in trust—Real estate and business opportunity transactions.

The procedures in this section are applicable to funds received by the firm in connection with real estate sales, business opportunity transactions or options. These procedures are in addition to the requirements of the general trust account procedures contained in WAC 308-124E-105.

(1) Bank accounts, deposit slips, checks and signature cards shall be designated as trust accounts in the firm or assumed name as licensed. Trust bank accounts for real estate sales or business opportunity transactions shall be interest bearing demand deposit accounts. These accounts shall be established as described in RCW 18.85.285 and this section.

(a) The firm shall maintain a pooled interest-bearing trust account identified as housing trust fund account for deposit of trust funds which are ten thousand dollars or less. Interest income from this account will be paid to the department by the depository institution in accordance with RCW 18.85.285(8) after deduction of reasonable bank service charges and fees, which shall not include check printing fees or fees for bookkeeping systems.

(b) The licensee shall disclose in writing to the party depositing more than ten thousand dollars that the party has an option between (b)(i) and (ii) of this subsection:

(i) All trust funds not required to be deposited in the account specified in (a) of this subsection shall be deposited in a separate interest-bearing trust account for the particular party or party's matter on which the interest will be paid to the party(ies); or

(ii) In the pooled interest-bearing account specified in (a) of this subsection if the parties to the transaction agree in writing.

(c) (i) For accounts established as specified in (a) of this subsection, the designated broker will maintain an additional ledger with the heading identified as "Housing trust account interest." As the monthly bank statements are received, indicating interest credited, the designated broker will post the amount to the pooled interest ledger. When the bank statement indicates that the interest was paid to the state or bank fees were charged, the designated broker will debit the ledger accordingly.

(ii) For accounts established as specified in (b)(i) of this subsection, the interest earned or bank fees charged will be posted to the individual ledger.

(d) When the bank charges/fees exceed the interest earned, causing the balance to be less than trust account liability, the designated broker shall within one banking day after receipt of such notice, deposit funds from the firm's business account or other nontrust account to bring the trust account into balance with outstanding liability. The designated broker may be reimbursed by the party depositing the funds for these charges for accounts established as specified in (b)(i) of this subsection if the reimbursement is authorized in writing by the party depositing the funds. For accounts established under (a) of this subsection, the designated broker will absorb the excess bank charges/fees as a business expense.

(2) A separate check shall be drawn on the real estate trust bank account, payable to the firm as licensed, for each commission earned, after the final closing of the real estate or business opportunity transaction. Each commission check shall be identified to the transaction to which it applies.

(3) No disbursements from the real estate trust bank account shall be made in advance of closing of a real estate or business opportunity transaction or before the happening of a condition set forth in the purchase and sale agreement, to any person or for any reason, without a written release from both the purchaser and seller; except that:

(a) If the agreement terminates according to its own terms prior to closing, disbursement of funds shall be made as provided by the agreement without a written release; and

(b) Funds may be disbursed to the escrow agent designated in writing by the purchaser and seller to close the transaction, reasonably prior to the date of closing in order to permit checks to clear.

(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 licensee shall deliver the earnest money deposit to the party designated by the terms of the purchase and sale agreement to hold the funds. The licensee shall obtain a dated receipt from the party holding the earnest money funds. The licensee shall deliver the receipt to the designated broker or responsible managing broker. The dated receipt shall be placed in and retained in all participating firm's transaction files. The designated broker has the ultimate responsibility for delivery of the funds.
APPENDIX D

WAC 308-124E-115 Administration of funds held in trust—Property management.

These procedures are applicable to property management and contract/mortgage collection agreements, and are in addition to the general trust account procedures in WAC 308-124E-105.

(1) Trust bank accounts for property management transactions are exempt from the interest-bearing requirement of RCW 18.85.285. However, interest-bearing accounts for property management transactions may be established as described in this section.

   (a) Interest-bearing trust bank accounts or dividend-earning investment accounts containing only funds held on behalf of an individual owner of income property managed by the firm may be established when directed by written property management agreement or directive signed by the owner: Provided, That all interest or earnings shall accrue to the owner;

   (b) Interest-bearing trust bank accounts containing only damage or security deposits received from tenants of residential income properties managed by the firm for an individual owner may be established by the designated broker when directed by written management agreement, and the interest on such trust bank accounts may be paid to the owner, if the firm is by written agreement designated a "representative of the landlord" under the provisions of RCW 59.18.270, Residential Landlord-Tenant Act;

   (c) The designated broker is not required to establish individual interest-bearing accounts for each owner when all owners assign the interest to the firm;

   (d) A common account, usually referred to as a "clearing account" may be established if desired. This account must be a trust account.

(2) Any property management accounting system is to be an accounting of cash received and disbursed. Any other method of accounting offered to owners for their rental properties, unit and/or complexes are to be supplementary to the firm’s accounting of all cash received and disbursed through the firm’s trust account(s). All owners’ summary statements must include this accounting.

(3) The preauthorization of disbursements or deductions by the financial institution for recurring expenses such as mortgage payments on behalf of the owner is not permitted if the account contains tenant security deposits or funds belonging to more than one client.

(4) A single check may be drawn on the real estate trust bank account, payable to the firm as licensed, in payment of all property management fees and commissions, if such check is supported by a schedule of commissions identified to each individual client. Property management commissions shall be withdrawn at least once monthly.

(5) No disbursements from the real estate trust bank account shall be made of funds received as damage or security deposit on a lease or rental contract for property managed by the firm to the owner or any other person without the written agreement of the tenant, until the end of the tenancy when the funds are to be disbursed to the person or persons entitled to the funds as provided by the terms of the rental or lease agreement.

(6) When the management agreement between the owner(s) and the firm is terminated, the owner(s) funds shall be disbursed according to the agreement. Funds held as damage or security deposits shall be disbursed to the owner(s) or successor property manager, and the tenants so notified by the disbursing firm consistent with the provisions of RCW 59.18.270, Residential Landlord-Tenant Act.