



## What is Escrow?

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An escrow is an arrangement in which a disinterested third party, called an escrow holder, holds legal documents and funds on behalf of a buyer and seller, then distributes them according to the buyer's and seller's instructions. People buying and selling real estate often open an escrow for their protection and convenience. The buyer can instruct the escrow holder to disburse the purchase price only upon the satisfaction of certain prerequisites and conditions. The seller can instruct the escrow holder to retain possession of the deed to the buyer until the seller's requirements — including receipt of the purchase price — are met. Both rely on the escrow holder to faithfully carry out their mutually consistent instructions relating to the transaction and to advise them if any of their instructions are not mutually consistent or cannot be carried out. An escrow is of particular importance for both the buyer and seller because they can move forward separately but simultaneously in providing inspections, reports, loan commitments and funds, deeds, and many other items, using the escrow holder as the central depositing point. If the instructions from all parties to an escrow are clearly drafted, fully detailed and mutually consistent, the escrow holder can take many actions on their behalf without further consultation. This saves much time and facilitates the closing of the transaction.

### Who May Hold an Escrow?

The escrow holder may be any disinterested third party (although some states require that certain escrow holders be licensed). There are important reasons for selecting an established, independent escrow firm, an attorney, or an escrow officer with a bank, S&L or title insurance company. One is that real estate transactions require a tremendous amount of technical experience and knowledge to proceed smoothly. The other is that the escrow holder will generally be responsible for safeguarding and properly distributing the purchase price. Escrow officers with established firms generally are experienced and trained in real estate procedures, title insurance, taxes, deeds and insurance.

### Impartiality

An escrow officer must remain completely impartial throughout the entire escrow process. He or she will normally adopt a courteous but rather formal manner when dealing with all parties involved in the escrow, keeping conversation to the matters at hand. This formal behavior is meant for the benefit of all concerned, since the officer must follow the instructions of both parties without bias.

### Escrow Instructions

Escrow instructions are written documents, commonly known as purchase and sale agreements, signed by the parties giving them, which direct the escrow officer in the specific steps to be completed, so the escrow can be closed.

Typical instructions would include the following:

- the method by which the escrow holder is to receive and hold the purchase price to be paid by the buyer
- the conditions under which a lapse of time or breach of purchase contract provision will terminate the escrow without a closing
- the instruction and authorization to the escrow holder to disburse funds for recording fees, title insurance policy, real estate commissions, and any other closing costs incurred through escrow
- instructions as to the pro-ration of insurance and taxes
- instruction to the escrow holder on the payment of prior liens and charges against the property and distribution of the net sale proceeds

Since the escrow holder can only follow the instructions as stated, and may not exceed them, it is extremely important that the instructions be stated clearly and be complete in all details.

## What Each Party Does in the Escrow Process

### *The Seller:*

- deposits the executed deed to the buyer with the escrow holder
- deposits evidence of pest inspection and any required repair work
- deposits other required documents such as tax receipts, addresses of mortgage holder, insurance policies, equipment warranties or home warranty contracts, etc.

### *The Buyer:*

- deposits the funds required, in addition to any borrowed funds, to pay the purchase price with the escrow holder
- deposits funds sufficient for home and title insurance
- arranges for any borrowed funds to be delivered to the escrow holder
- deposits any deed of trust or mortgages necessary to secure loans
- approves any inspection reports, title insurance commitments, etc. called for by the purchase and sale agreements
- fulfills any other conditions specified in the escrow instructions

### *The Lender (if applicable):*

- deposits proceeds of the loan to the purchaser
- directs the escrow holder on the conditions under which the loan funds may be used

### *The Escrow Holder:*

- opens the order for title insurance
- obtains approvals from the buyer on title insurance report, pest and other inspections
- receives funds from the buyer and/or lender
- prorates insurance, taxes, rents, etc.
- disburses funds for title insurance, recording fees, real estate commissions, lien clearance, etc.
- prepares a final statement for each party indicating amounts to be disbursed for services and any further amount necessary to close escrow
- records deeds and loan documents, and delivers the deed to the buyer, loan documents to the lender and funds to the seller, thereby closing the escrow

## Closing the Escrow

Once all the terms and conditions of the instructions of both parties have been fulfilled, and all closing conditions are satisfied, the escrow is closed and the safe and accurate transfer of property and money is completed.

## Division of Charges

The method of dividing the charges for the services performed through escrow, or as a result of escrow, varies from place to place. The fees and service charges to be divided might include, for example: the title insurance policy premium, escrow fee, any transfer taxes, recording fees, and costs in connection with any loan being obtained. Unless there is some special agreement between the buyer and seller as to how these charges are to be paid, local custom will generally be followed in drafting the instructions to the escrow holder as to how they are to be divided.

## In Summary

The escrow process was developed to help facilitate the sale or purchase of your home. The escrow holder accomplishes this by:

- acting as the impartial "stakeholder", or depository of documents and funds
- processing and coordinating the flow of documents and funds
- keeping all parties informed of progress on the escrow
- responding to the lender's requirements
- securing a title insurance policy
- obtaining approvals of reports and documents from the parties as required
- prorating and adjusting insurance, taxes, rents, etc.
- recording the deed and loan documents
- maintaining security and accountability of monies owed and owing

## It's Not Always This Simple

The examples and explanations described here are designed to acquaint you with the escrow process and are based on relatively simple escrows. Every escrow is unique and most are more complex than explained here. If you have questions about the escrow process, we suggest you contact an escrow officer or attorney to obtain detailed advice and further explanation.