

**CALIFORNIA ESCROW LAW AUDIT REPORT**

DFPI-EL 315 (Rev. 11-20)



I. Preparation of Independent Audit Report - 1741.5 (a) (CCR)

(1) The Independent Annual Audit Report shall be prepared in accordance with the provisions of Section 17406 of the Escrow Law, and as provided in the paragraphs of this subsection. For determining independence, the regulations of the California State Board of Accountancy (Chapter 1, Sections 1 through 99.1, Title 16, California Code of Regulations) shall apply.

(2) The following items shall be considered in preparation of the report and in examining the financial statements included in the annual report:

(A) If the licensee is engaged in other businesses, in addition to the escrow business, the financial statements of the licensee shall include the assets and liabilities employed in such other businesses and the results of the operations thereof.

(B) The income statement shall state, separately from other salaries, the amount of salaries and bonuses paid to officers.

(C) If the liabilities include long term notes or mortgages, the amount of monthly payments, name of payee, due date, and other terms and conditions, including any subordination agreement which may exist with respect thereto in the financial statements or a footnote thereto, shall be stated.

(D) Quoted market values, if available, shall be stated parenthetically on the balance sheet or in a supporting schedule for such items as marketable securities, including obligations of the United States Government, bonds of state and municipal governmental units, etc. A schedule of all securities shall be included in the annual report.

(E) The report shall contain a statement as to whether the licensee met the liquid asset and tangible net worth requirement of Section 17210 of the Financial Code on the balance sheet date. The report shall include:

(i) A schedule showing the computation of both the licensee's liquidity and tangible net worth for measuring compliance with Section 17210 of the Financial code.

(ii) An itemized schedule listing each item included in the computations.

(iii) If marketable investments are included as liquid assets, the following information must be shown: company name; market value at balance sheet date; cost; the name of the exchange it is listed on; and the stock symbol.

(iv) If fees receivable is to be considered a liquid asset, a copy of the fee ledger at the balance sheet date must be included with the report.

(F) The report shall include copies of the trust bank account reconciliations for each location as of the balance sheet date, including all interest bearing and dormant accounts. The report shall contain an outstanding checklist which includes check and escrow numbers, dates and amounts for each check and an explanation for all adjustments and reconciling items including the date of adjustment. This explanation shall include an affirmative statement if any reconciling items were not adjusted as of the report date and whether the adjustments cause debit balances (shortages). The outstanding checklists submitted with the audit report shall be maintained in the confidential section of the Department of Financial Protection and Innovation's records.

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- (G) The report shall include an escrow trial balance as at the reconciliation date.
- (H) The report shall disclose if the licensee is engaged in the business of receiving escrows for deposit or delivery of the types of transactions specified in subdivision (c) of Section 17312 of the Financial Code and if the licensee is engaged in the business of receiving escrows for deposit or delivery of the types of transactions not specified therein, or both. If applicable, the report shall include:
  - (I) A trial balance for the types of transactions specified in subdivision (c) of Section 17312 of the Financial Code and a separate trial balance for the types of transactions not specified therein. The trial balances submitted with the audit report shall be maintained in the confidential section of the Department of Financial Protection and Innovation’s records.
  - (ii) A statement whether escrow books and escrow trust accounts are maintained for those transactions specified in subdivision (c) of Section 17312 of the Financial Code separate from those transactions not specified therein.
  - (iii) If the escrow agent is engaged in the business of receiving escrows for deposit or delivery of the types of transactions not specified in subdivision (c) of Section 17312 of the Financial Code, a statement shall be made whether the licensee has fidelity bond coverage as required by Section 1723 of these rules.
  - (iv) If the escrow agent is engaged in the business of receiving escrows for deposit or delivery of the types of transactions specified in subdivision (c) of Section 17312 of the Financial Code, a statement shall be made whether the licensee is a member of Escrow Agents’ Fidelity Corporation as required by Section 17312 of the Financial Code.
- (3) The report shall include a statement indicating:
  - (A) That the individual escrow liability accounts and the controlling account have been reconciled to the escrow trust account as at the balance sheet date. If debit balances exist in the escrow liability, a full explanation of the nature and cause of the debit balances must be included in the auditor’s comments along with a full explanation of the resolution of the item. If the debit balance has not been resolved as of the date of the auditor’s report, then the auditor shall include a positive statement stating that the debit balance has not been resolved as of the auditor’s report date. If no debit balances were in existence at the balance sheet date, a positive statement of this fact shall be made; and
  - (B) That the escrow funds were independently confirmed in writing by the accountant directly with the depositories or other holders of escrow assets.
- (4)(A) The schedule of the escrow liability as at the end of each month during the calendar or fiscal year as reflected in the Escrow Control Account must be included in the report.
- (B) If the audit is commenced on a date other than the calendar or fiscal year-end, the accountant shall request cut-off bank statements on all bank accounts covering the period from the balance sheet date to the date the audit is commenced. The bank accounts shall be reconciled to adjusted book balances as at the cut-off date, with particular attention given to the propriety and disposition of reconciling items appearing in the bank reconciliations at the balance sheet date. The report shall include and show the same information as at the cut-off date as is required by subsection (4) of this subsection.

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- (5) The opinion or report of the independent accountant shall include a statement to the effect that the accountant has examined the financial statements with respect to the provisions of Part 3, Title 10, of the Code of Civil Procedure, and the results of such examination.
- (6) The accountant shall use such additional auditing procedures and standards including extension of the minimum escrow liability confirmation required above that is considered necessary in verifying the escrow funds and the escrow liability. The escrow liability shall include all escrow funds deposited into interest-bearing accounts pursuant to Section 1737 (b). The comments shall include details of the nature and extent of all additional auditing procedures used in this verification.
- (7) The following additional procedures shall be performed, and the results shall be disclosed in the report:
  - (A) Verify the authorization and documentation of disbursements from a selective number of escrows.
  - (B) Select a representative sampling of escrows closed within 60 days prior to the commencement of the audit and perform the following audit procedures:
    - (I) Review escrow instructions, correspondence and documents in the escrow files for authorization of disbursements.
    - (ii) Review checks for disbursements out of escrow.
  - (C) Review the schedule of escrow liability as of the last audit for dormant files and outstanding checks and perform the following audit procedures:
    - (I) Verify that funds in the oldest dormant files that no longer are on the schedule of escrow liability were properly disbursed according to signed instructions or according to the instructions of a court of competent jurisdiction, were interpleaded to a court of competent jurisdiction, or were escheated to the State of California. The selection of dormant files shall include those that were older than six months at the last audit and no longer appear on the current schedule of escrow liability.
    - (ii) Verify that the oldest dormant outstanding checks that no longer appear on the outstanding checklist were paid, were properly canceled back into the escrow fund, were properly canceled and re-issued to the original payee, were properly canceled and re-issued to a new payee according to instructions or were escheated to the State of California. The selection of the checks shall include those checks that were older than six months at the last audit and no longer appear on the current outstanding checklist. The procedures shall include the review of check endorsements.
- (8) When a licensee has branches, a statement shall be made by the accountant that the examination included auditing of the branches, and the address of each branch examined shall be listed.
- (9) If in the opinion of the independent public accountant a departure from the requirements set forth in this section is justified, upon request, the Commissioner may grant a variance upon a proper showing of suitable alternative procedures.

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II. Audit Reports and Financial Statements - 17406 (FC)

(a) Each Licensee shall submit to the commissioner, at such licensee's own expense, an audit report containing audited financial statements covering the calendar year or, if such licensee has an established fiscal year, then for such fiscal year, within 105 days after the close of each such calendar or fiscal year. At such time, each licensee shall also file such additional relevant information as the commissioner may require.

(b) Within 30 days after receipt of a request from the commissioner, a licensee or other person subject to this division shall submit to the commissioner, at such person's own expense, an audit report containing audited financial statements covering the 12 calendar months next preceding the month of receipt of the request, or such other period as the commissioner may require. Unless the public interest shall otherwise require, the commissioner shall exempt a licensee from the provisions of subdivision (a) hereof in whole or in part if such licensee has complied with a request pursuant to this subdivision as of a date within the calendar or fiscal year for which such exemption is granted.

(c) A licensee whose license has been surrendered or revoked shall submit to the commissioner, at its own expense, on or before 105 days after the effective date of such surrender or revocation, a closing audit report as of such effective date, or for such other period as the commissioner may specify. Such report shall include the information specified by the commissioner. A licensee who has complied with this subdivision is exempted from subdivision (a) of this section.

(d) The reports and financial statements referred to in subdivision (a), (b), and (c) of this section shall include at least a balance sheet and a statement of income for the year ended on the balance sheet date together with such other relevant information as the commissioner may require, and shall be prepared in accordance with generally accepted accounting principles, and shall be accompanied by a report, certificate, or opinion of, an independent certified public accountant or independent public accountant. The audits shall be conducted in accordance with generally accepted auditing standards and the rules of the commissioner.

(e) A licensee shall make other special reports to the commissioner as the commissioner may from time to time require.

(f) For good cause and upon written request, the commissioner may extend the time for compliance with subdivisions (a) and (b) of this section.

(g) A licensee shall, when requested by the commissioner, submit its unaudited financial statements, prepared in accordance with generally accepted accounting principles and consisting of at least a balance sheet and statement of income and expense as of the date and for the period specified by the commissioner. The commissioner may require the submission of such reports on a monthly or other periodic basis.

(h) If the report, certificate, or opinion of the independent accountant referred to in subdivision (d) hereof is in any way qualified, the commissioner may require the licensee to take such action as he deems appropriate to permit an independent accountant to remove such qualifications from the report, certificate or opinion.

(i) The commissioner may reject any financial statement, report, certificate or opinion by notifying the licensee or other person required to make such filing of its rejection and the cause thereof. Within 30 days after the receipt of such notice, the licensee or other person shall correct such deficiency and the failure so to do shall be deemed a violation of this division. The commissioner shall retain a copy of

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all filings so rejected.

(j) The commissioner may make rules specifying the form and content of the reports and financial statements referred to in this section and may require that such reports and financial statements be verified by the licensee in such manner as he may prescribe.

(k) Upon completion of the reports and financial statements referred to in subdivision (a), (b), and (c), the independent accountant shall submit to the commissioner complete copies of the reports and financial statements while copies of the reports and financial statements are submitted to the licensee.

III. Reports or Certification of Reports and Financial Statements by Another Accountant; Disagreements; Licensee's Written Notice to Commissioner; Letter from Former Accountant - 17406.1 (FC)

(a) Whenever the reports and financial statements required pursuant to subdivision (a), (b), or (c) of Section 17406 are to be reported upon or certified by an accountant other than the accountant reporting upon or certifying the licensee's most recent reports or financial statements, the licensee shall furnish the commissioner with a written notice stating whether there was any disagreement with the former accountant on any matter in connection with the preparation of the most recent reports or financial statements reported upon or certified by that former accountant. If there was any disagreement, the licensee's written notice shall describe the reasons for the disagreement. The written notice shall be signed by the chief executive officer of the licensee. The licensee shall also request, in writing, that the former accountant furnish the licensee with a letter addressed to the commissioner stating whether the former accountant agrees with the statements contained in the licensee's written notice. If the former accountant disagrees with any of the licensee's statements, the former accountant's letter shall explain the reasons for disagreeing with the licensee's statements. The written notice of the licensee, along with the former accountant's letter shall be filed with the commissioner no later than 30 days from the date of engagement of the new accountant.

(b) The written notice of the licensee required by subdivision (a) shall be considered a notice for purposes of Section 17702.

The instructions above are intended as a guide only. The CPA is responsible for issuing a report that adequately discloses the findings of the audit and is in conformance with Generally Accepted Auditing Standards.