

May 26, 2023: Ensuring That Your Trust/Escrow Accounts Are Treated As Fiduciary Accounts

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The Division of Real Estate has been receiving ongoing questions and concerns from both real estate brokers as well as financial institutions regarding the requirements for real estate brokers engaging in property management or holding money belonging to others to establish a trust or escrow account. The Division has seen many instances where a real estate broker opens a bank or credit union account for the purpose of holding money belonging to others where the account label contains the word, “trust or escrow;” however, the account is not an actual trust or escrow account. This is problematic and can result in lost consumer funds due to, but not limited to, the following examples including lawsuits, bankruptcies, overdraft/account setoffs, legal garnishments, and bank or credit union failures.

To protect consumers, the Colorado Real Estate Commission has the following statutes and rules regarding money belonging to others, including, but not limited to:

- § 12-10-217(1)(i), states, “Converting funds of others, diverting funds of others without proper authorization, commingling funds of others with the broker’s own funds, or **failing to keep the funds of others in an escrow or a trustee account with some bank or recognized depository in this state**, which account may be any type of checking, demand, passbook, or statement account insured by an agency of the United States government, and to keep records relative to the deposit that contain such information as may be prescribed by the rules of the commission relative thereto, which records shall be subject to audit by the commission.”
- Rule 5.2 “Trust or Escrow Accounts” states in part, “All Money Belonging to Others accepted by a Broker or Brokerage Firm for deposit into the Broker’s or Brokerage Firm’s Trust or Escrow Account must be deposited in one or more accounts separate from other money belonging to the Broker or Brokerage Firm.”
- Rule 5.11.A.2. “Money Belonging to Others for deposit by a Broker for Non-Real Estate Brokerage Services” states in part, “Money Belonging to Others which is accepted for deposit in connection with activities not involving Real Estate Brokerage Services must be deposited into Broker’s or Brokerage Firm’s Trust or Escrow Account(s). Such activities not involving Real Estate Brokerage Services include: Security deposits for Broker’s own rental properties including

any Broker owned properties held in a partnership, or other entity with others, any joint ventures, or syndications provided the Broker's ownership in the entity or property is more than the 20% threshold pursuant to section 12-10-201(6)(b)(VII), C.R.S."

- Rule 1.44 defines a "Recognized Depository" as "Any bank, savings and loan association, or credit union that accepts deposits or shares insured by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA) respectively."
- Rule 1.55 defines a "Trust or Escrow Account" as "Any checking, demand, passbook, or statement account, which has, at a minimum, the following elements: A. The account is separate and contains only Money Belonging to Others; B. **The account is custodial and fiduciary**; C. All funds are available on demand; and D. The account is held with a Recognized Depository."

The Federal Deposit of Insurance Corporation (FDIC) defines a fiduciary account as, "Fiduciary accounts are deposit accounts established by a person or entity for the benefit of one or more other parties, also known as principals. The deposit account can be established for the benefit of a single owner, or a commingled account may be established for the benefit of multiple owners. The individual or entity opening the account does not have an ownership interest in the deposit." Furthermore, the FDIC provides examples of these types of accounts which includes "real estate and other escrow accounts." The FDIC also states, "Deposits held by a fiduciary on behalf of one or more principals are insured on a passthrough basis as the deposits of the principal (the actual owner) to the same extent as if the deposits were deposited directly by the principal, provided all of the following three requirements are met: (1) Funds must be in fact owned by the principal and not by the third party who set up the account (i.e., the fiduciary or custodian who is placing the funds). (2) The insured depository institution's (IDI) account records must indicate the agency nature of the account (e.g., XYZ Company as Custodian, XYZ For the benefit of (FBO), Jane Doe UTMA [**Uniform Transfers to Minors Act Account**] John Smith, Jr.); and (3) The records of the IDI, the fiduciary or a third party must indicate both the identities of the principals as well as the ownership interest in the deposit." "Fiduciary relationships include, but are not limited to, arrangements involving: a trustee; an agent; a nominee; a custodian; and a guardian."

Regarding deposit insurance, the FDIC states, "Agency accounts are not a separate ownership category. As detailed in this section, accounts held by a fiduciary, provided all the requirements are met, are insured based on the actual ownership of the funds. Therefore, fiduciary accounts are added to a depositor's other accounts in the same ownership category at the same IDI. The manner in which the funds are deposited, whether directly by the actual owner or through a custodian, agent, or broker, does not impact aggregation. In other words, since fiduciary accounts are not a separate ownership category, deposit insurance coverage is determined based on the ownership capacity in which the funds are held. For example, if a fiduciary, such as a broker, has opened a single account on behalf of Barry Richards in XYZ Bank and Barry

Richards directly opens another single account directly with XYZ Bank, both of these deposits are combined and insured for up to \$250,000.”

The FDIC also warns that, “If the disclosure and the recordkeeping requirements discussed in this section are not met, the accounts will be insured as the deposits of the fiduciary in either the single account or corporate account category. These deposits will then be added to any other deposits the fiduciary may hold in the same ownership category at the same IDI, and the total will be insured up to \$250,000.”

Real estate brokers licensed in Colorado that are holding money belonging to others need to pay extra attention to the accounts they open at financial institutions to avoid unnecessary license law violations. Brokers and their financial institutions need to understand that the funds in these accounts do not belong to the brokers. These accounts cannot be subject to any legal actions including wage garnishments, lawsuits, and bankruptcy proceedings against the broker. Additionally, these accounts cannot have any right to be set off, including overdrafts, or unpaid loan balances, etc. Lastly, if these accounts are set up properly, the individual principals or beneficiaries of the account will have some, if not complete, deposit insurance protection in the event of a financial institution failure.

If these accounts are opened correctly, they will ensure that their clients, property owners, and tenant's funds are protected.

Please visit the Division of Real Estate’s [Separate Accounts and Accounting page](#) on its website for examples of proper trust and escrow signature cards, statutory and rule compliant notices that may be presented to the banking institution, and a list of institutions that have confirmed with the Division that they offer true trust and escrow accounts.

References:

- State of Colorado Department of Regulatory Agencies, Division of Real Estate. (2023). Colorado Real Estate Manual (2023 ed.). LexisNexis Matthew Bender & Company, Inc.
- Federal Deposit of Insurance Corporation, FDIC. (February 24, 2023) (Last Updated). Financial Institution Employee’s Guide to Deposit Insurance. <https://www.fdic.gov/resources/deposit-insurance/diguidebankers/documents/fiduciary-accounts.pdf>