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Escrow

Escrow Defined

Escrow is the deposit of funds or another instrument by one party to be delivered to another party upon the completion of specified terms set by both parties. All terms must be met before the funds are released. Escrow accounts are neutral and protect the interests of all involved parties.

Real estate transactions are an excellent example of escrow. In a real estate transaction, a buyer and seller who have agreed on the sale of a piece of property may set up an escrow account. They will then establish terms and conditions for the transfer of ownership of that property. The terms and conditions are given to a third, neutral party, with no interest in the transfer. The neutral party is called the escrow holder. The escrow holder is responsible for making sure that all terms are carried out. In real estate, the escrow is where all monies, contracts, and other documents are stored for the sale of a home. This includes the down payment, the deed, and any other required documents. An escrow can also be used as a trust account held in a borrower's name to pay obligations like property taxes and insurance premiums when a new homeowner takes out a mortgage.

What Does An Escrow Do For You?

An escrow provides a guarantee that no property or funds will be exchanged until all terms and conditions of an agreement have been met. The escrow holder must watch over the funds and documents and pay out the funds and handle the title transfer when all requirements of the escrow are complete.

How does the Escrow Process Work?

The interested parties create escrow instructions. They sign and deliver the instructions to the escrow holder. One party deposits funds with the escrow holder. The escrow holder then processes the escrow according to the escrow instructions. When all escrow conditions are met, the other party receives the funds and the escrow is closed.

The escrow holder protects the interests of both parties using the guidelines outlined within the escrow instructions. Escrow cannot be completed until all conditions have been satisfied and all parties have signed off on the escrow documents.

The duties of the escrow holder include:

- Managing the funds and documents as outlined in the escrow agreement.
- Paying any bills as authorized.
- Responding to requests from the interested parties.
- Closing the escrow after all conditions are met.
- Distributing funds per the instructions.

How is an Escrow Opened?

An interested party will open an escrow. An escrow account is established at a financial institution. After the completion of an agreement and/or sale between the parties, funds are deposited into the escrow account.

How Does An Escrow Closing Work?

An escrow closing finalizes the transaction. It signifies legal transfer of funds from the buyer to the seller. In real estate, the grant deed is normally recorded within one working day of the escrow holder's receipt of loan funds. After all of the conditions of the escrow have been satisfied, the escrow holder will inform the parties of the escrow closing and handle all of the technical and financial details. In real estate, final closing papers are disbursed at the close of escrow after the escrow holder confirms that the documents have been recorded at the county records office.

Internet Escrow

Internet escrow was introduced when Internet commerce and Internet auctions came about. It established trust between parties when conducting online transactions.

Internet escrow puts money under the control of an independent and licensed third party. This insures that both parties are protected in the transaction. In Internet escrow, the parties must confirm that the transaction has been completed according to the agreed upon instructions before the money is released. If there is disagreement between the parties, the process must go into dispute resolution. The dispute resolution process determines what happens to any funds in escrow.

Fraudulent escrow scams have been used online. In some cases, scammers suggest the use of a third-party escrow service to lure their victim into feeling secure. The victim will have no idea that the scammer created an escrow site that looks like a real escrow service. The victim then is lured into sending a payment to the scam escrow company and never receives the item they paid for. Sometimes they flip the scam and have the victim send an item to the scammer, and in this case the victim waits to receive payment from the escrow site, which they never receive because the site is a scam. Legitimate online escrow companies are listed on a government register. All parties should verify an online escrow service using the online government register before conducting any transactions. There is no license offered by the US Federal Government for online escrow services. Some states do offer a license for online escrow services.

Trusts

Trusts Defined

A trust is used to minimize estate taxes and offer other benefits as part of a carefully designed estate plan.

A trust is a fiduciary agreement that allows a third party (a trustee) to hold assets on behalf of a beneficiary or beneficiaries. There are numerous ways to set up a trust and they can be used to define exactly how and when assets pass to beneficiaries.

Trusts usually allow an estate to bypass probate. Beneficiaries usually gain access to assets more quickly than they would if the assets were transferred using a will. If an irrevocable trust is used, it may not be considered part of the taxable estate, thus lowering taxes due upon the holder of the trust upon death.

A trust also allows assets to be passed outside of probate, which saves time, court fees, and possibly estate taxes.

Trusts allow for:

Wealth Control – Wealth is controlled by explicitly specifying the terms of the trust. This allows controlling when, and to whom, distributions are made. A revocable trust allows for trust assets to remain accessible during the trust holder's lifetime and the ability to designate to whom remaining assets will pass.

Legacy protection - A carefully created trust can protect an estate from the creditors of heirs and beneficiaries that have poor wealth management skills.

Privacy and probate savings - With a trust, assets may pass outside of probate and remain private. Probate becomes public record. This also helps to reduce assets lost to court fees and taxes from the probate process.

Revocable and Irrevocable Trusts

Revocable Trusts

A revocable trust is sometimes called a living trust. It allows assets to pass outside of probate, but also allows the trust holder (grantor) to retain control of the assets during his/her lifetime. It can be dissolved at any time if the situation or intentions change. Generally, a revocable trust becomes irrevocable upon the death of the grantor.

The grantor can name him/her-self trustee (or co-trustee) and keep ownership and control of the trust. The grantor may make provisions for a successor trustee in the event of his/her death or inability to function as a trustee.

Revocable trusts usually help to avoid probate, but are still subject to estate taxes. While the grantor is alive it is treated like any other asset he/she owns.

Irrevocable Trusts

An irrevocable trust transfers assets out of the grantor's estate and possibly out of the reach of estate taxes and probate. However, it cannot be altered by the grantor after execution. Once this type of trust is established the grantor loses control over the assets and cannot change the terms or dissolve the trust. Irrevocable trusts are usually preferred over revocable trusts if the primary goal is to reduce the amount of assets subject to estate taxes. It removes trust assets from the estate. Since the assets have been transferred to the trust, the grantor is free from the tax liability on the income generated by the trust assets. Irrevocable trusts can also protect assets if there is ever a legal judgment against the grantor.

Types of Trusts

Tax By-Pass Trust

A Tax By-Pass Trust allows one spouse to leave money to the other and limits the amount of Federal Estate tax that would be payable on the death of the second spouse. Although assets can pass to a spouse without being taxed, when the surviving spouse dies, any assets left above the exempt limit are taxable to the children of the couple. A Tax By-Pass Trust protects the assets from taxation in this situation.

Totten Trust

In a Totten Trust, the grantor deposits money into an account at a financial institution in his or her name as the trustee for another. This is a revocable trust and the gift is not completed until the grantor dies. The beneficiary can be an individual or an entity. The Totten Trust keeps assets from probate. It is normally used with bank accounts and CDs. However, this type of trust cannot be used with real property. Totten Trusts are safer for passing assets on to family than joint ownership accounts. A Totten Trust is also known as a "poor man's" trust because there is no written document and usually costs the trust maker nothing to create.

Spendthrift Trust

This is a trust that will not allow the beneficiary to sell interests in the Trust. It is protected from the creditors of the beneficiaries until assets are distributed out of the trust to the beneficiaries.

Constructive Trust

A Constructive Trust is an implied trust established by the court. The court assesses the situation and determines the guidelines for the trust. For example, if there was not a formal declaration of a trust, the court may decide that there was an intention for assets or property to go to a particular person.

Special Needs Trust

A Special Needs Trust is set up for a person receiving government benefits and prevents a beneficiary from being disqualified from future government benefits due to increased assets. By law, the disabled beneficiary is not allowed to control the amount or frequency of trust distributions. The beneficiary cannot revoke the trust.

Special needs has a legal definition and is defined as the requirements for maintaining the comfort and happiness of a disabled person, when these requirements are not being provided by government benefits. These trusts can cover medical and dental expenses, education, treatment, eyeglasses, transportation, insurance, and other similar needs. Parents can establish a special needs trust for disabled children as part of their estate plan. Disabled persons expecting an inheritance can create a special needs trust themselves, but cannot name themselves as trustee.

Asset Protection Trust

An Asset Protection Trust protects assets from claims of future creditors. These are usually set up outside of the United States. These trusts insulate assets from creditors. They are usually irrevocable for a term of years so that the trust maker is not a current beneficiary. They are usually structured so that undistributed assets of the trust are returned to the trust maker when the trust is terminated if there is no risk of creditor attack.

Charitable Trust

Charitable Trusts benefit a charity or the public in general. They are usually established to lower or avoid imposition of estate and gift tax. Charitable Trusts also reward the trust maker sense of altruism.

Auctioneering & Escrow

Auctioneering Escrow Accounts

In auctioneering, an Escrow Account is a separate and distinct bank account used for holding other people's money. This includes money taken in from an auction sale for a client while the auctioneer waits for all funds to clear the bank – clearance could relate to credit cards, cash, or checks.

Why Should and Auctioneer Have an Escrow Account?

An auctioneer cannot mix their business funds and their client's funds. Generally, it is best for an auctioneer to have his or her own business bank account. From this account they pay their own bills, business expenses, and salaries. A completely separate escrow account should be used for money from auction sales being held for their clients. This keeps the auctioneer from ever using a client's money to pay his or her bills and also insures that the money is available for the client. In addition, it allows money to be easily tracked and keeps a record of transactions for both parties.

A Simple Example of an Auctioneer Escrow Account

An auctioneer holds an auction sale for multiple clients. After funds are generated from the auctions, they are deposited directly into the auctioneer's escrow account. There is usually a time limit that mandates when the funds must be deposited. Different states have different laws for the timetable in which funds must be deposited, so you must check your own state laws for this timetable. After the funds clear the bank, the auctioneer sends all clients a check for their goods from the escrow account (minus commissions and other expenses). Then, the auctioneer writes a check from the escrow account to his or her business for all commissions and expenses owed for auctioneering services.

How Long Does an Auctioneer Have to Pay a Client?

The auctioneer will have enough time to be sure that all monies clear the bank (that there are no bad checks or bad credit card payments). For the exact timetable you must check the law in your state.

Do Auctioneer's Have to Have an Escrow Account?

This also varies by state. In many cases the answer is yes, unless clients are paid immediately after the auction or there is a specific written contract stipulating payment terms. However, the escrow account protects both the auctioneer and his or her clients, so it is an excellent idea to use an escrow account. Failing to use an escrow account can expose an auctioneer to fraudulent payments. So, unless the auctioneer only accepts cash payments and pays clients immediately, it is best to use an escrow account.

A Detailed Example of Why It's Best to Use a Trust or Escrow Account

John's been an auctioneer for over 20 years. He owns and runs "John's Expert Auction" in Topeka, Nebraska.

He accepts consignments from Monday through Thursday and holds an auction every Friday starting at 3:00 PM.

John and his 14-year-old son Mark are securing the auction house one day.

Mark asks his dad, "Dad, why do all of the doors need high security locks on the auction house? How come we have a high tech security system? Why is there so much security lighting on our lot? The auction house is in the middle of nowhere, who would even know it was here to rob?"

John says, "Mark, it's part of our job to protect the things that our client's entrust to us. There are works of art, jewelry, and a lot of other high value items that we keep here. None of this stuff belongs to us it belongs to our clients. It's part of our duty as a business to protect what our clients have entrusted to us."

Mark nods in understanding.

Later that week, John's Friday auction pulls in about $20,000.

After the auction, John has his lead cashier give him the $20,000 in cash and checks. He puts the funds in a money bag and zips it shut.

As John and Mark are leaving the auction house, Mark asks his dad about the money.

"Dad, did you get $20,000 from the cashier? We only charge 25% commission, so that's about $15,000 too much," says Mark

"Son, it's more than our 25%. I just took all the money so that I can keep it safe at home in the file cabinet."

"Dad, that extra $15,000 belongs to our clients, just like their valuables. It doesn't belong to us. We will have to pay them that money from their settlement," says Mark

"You're right kiddo. I'll take it to the bank when I have time on Wednesday. I know Sally always wants to pick up her settlement on Friday in cash," says John.

"But Dad, We don't have a safe or a security system at home. Plus, everybody knows where we live. If we use high security locks, a security system and extra lighting to protect the valuables at the auction house property, shouldn't we also protect their money?" says Mark.

Mark is right on the money (what a pun!). Often auctioneers go to extreme means to protect the valuables of their clients, and then fail to use the same level of protection with money from the auction.

Just like auctioneers use high security locks, security systems, and security lighting to protect an auction house, it's just as important that auctioneers protect their client's money by using an escrow or trust account.

An escrow or trust account is an account used only for client's monies. This not only protects the money, but also makes it easy to keep personal and business funds separate. So, in John's case, Mark is correct, his dad should be putting the money into an escrow or trust account and not in the file cabinet at home.

Separating personal and business funds is extremely important for auctioneers. It protects from the inadvertent or intentional mixing of client monies with business or personal funds. Mixing personal and business funds is called the commingling of funds.

Auctioneering is mostly state regulated, and some states require the use of an escrow or trust account, while some do not. However, the money we're talking about here belongs to the client not the auctioneer, so there's no reason for an auctioneer not to use a trust account to secure client monies.

It should be noted that on July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law. This law, in part, permanently raised the standard maximum deposit insurance amount (SMDIA) to $250,000. This FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category.

As an auctioneer it is part of your job to protect your client's property and their money, there's no better way to protect their money than with an escrow or trust account.

Estate and Trust Auctions

Estate Auctions

Generally, an estate sale or auction is used to dispose of a substantial portion of the assets owned by a recently deceased person. Sometimes, a person intent on moving may use an estate auction to quickly dispose of their personal property.

The most common reason for an estate sale or auction is the death of the property owner. Generally the assets and personal property of the deceased are handled with a will or a trust. Often, beneficiaries want to turn the personal property of the deceased into cash and this can be quickly accomplished with an estate auction.

Estate auctions usually occur when:

- The heirs have no interest in the bulk of the deceased person's personal belongings.
- The heirs have no space for the belongings.
- The heirs disagree on the disposition of tangible property and a court has ordered the goods to be sold in an estate sale or auction with the money from the sale to be divided among the heirs.
- Sometimes the will of the deceased mandates the sale or auction of all assets.

An estate sale or auction also occurs when a property owner is moving or has moved into a new residence and has no room for the remaining personal property. This could be a standard move or a scale down move such as when an elderly person moves into an assisted living facility, a rest home or retirement community, or moves in with a family member.

Sometimes an estate sale or auction occurs because of a divorce, foreclosure, or relocation.

Estate sales are usually conducted by an estate sale professional or auctioneer for a percentage of the revenues. The estate is charged for advertising, marketing, research, labor, security, and any other necessities.

Some estate sales require a permit. Sometimes it is required to collect sales tax on the sold items. There may be limits as to how much advertising is allowed.

<u>The Estate Auction Process</u>

Estate auctions have a preview period. This can be the day before the auction and/or during the hours leading up to the start of the auction. The preview period gives potential bidders a chance to look around at what's for sale, check the condition of items, and make notes about items before the auction. Many times bidders will have the opportunity to bid on a "lot" of items. This could be a box, or a trunk, or a case of items. In some cases it can be a total surprise as to what will be found inside.

When buyers arrive at the auction they must register. For regulars, they must check in at the front desk and pick up a bidder card (a white card with a number on it). Newcomers will need to supply their full contact information and driver's license number. When the auction begins, many bidders will already have an idea of what they want from the estate because of the preview period. The bidders can sit or stand in view of the auctioneer as items are brought up one by one to be sold. Many times all of the items at an estate auction are not sold. Items that don't sell can be kept for another auction or donated to charities or other non-profit organizations.

The primary difference between an estate sale and an estate auction is that items at an estate sale are priced. Many times items that do not sell at an estate sale move on to an auction house to be sold.

Estate Liquidation Sales and Auctions

It may be necessary to hire a professional liquidator when dealing with a trust or estate sale or auction. A liquidator will have knowledge and experience pricing the items in the estate and will have a good knowledge of household goods and personal property values. Liquidators often take from 20% to 50% of the net proceeds for their services.

Liquidations are similar to estate sales and auctions in that they often include selling the estate (home, garage, etc.) but they also include selling the contents of safe deposit boxes, family heirlooms, other real estate, vehicles, RV's, livestock, things that can be part of a trust such as stocks and securities, and other extraneous assets of the estate.

In most states, it is necessary for a realtor to be involved with the sale of land. Also, the family generally has a lawyer involved to make sure the paperwork and legal aspects are fully covered. Lawyers are also helpful when dealing with stocks, bonds, and investments that are being liquidated. However, it is usually not necessary to have a license or permit for selling the other types of items in a liquidation auction.

A primary difference between a liquidation sale or auction and an estate sale or auction is the involvement of stocks, bonds, coins, jewelry, other real estate property, and valuables that require appraisal. Additionally, professionals involved in a liquidation sale or auction generally require the services of realtors, attorneys, accountants, and appraisers. An estate auction does not usually require those professional services.

Business Liquidation Auctions

When a business closes its doors or an individual files for bankruptcy the involved parties may institute a liquidation auction. This is usually done when entities are in a state of financial flux and need to earn some cash for their goods. Liquidation auctions also come into play when the involved parties in a closing business or bankruptcy case would rather make a percentage off their holdings as opposed to holding onto their inventory.

In these cases, a liquidation auction is held and all items are sold at a heavily discounted price. The primary disadvantage to bidders in a business liquidation auction is that there are no warranties or refunds on the items. Items, thus, are sold as is. Usually, as the auction continues, the items decrease in quality.

Business liquidation auctions are governed by city and state licenses and require the seller to file an application and submit a list of the entire inventory. Businesses can bring additional items to the sale after submitting the approved inventory list. The city or state places a limit on how long the liquidation auction will last.

Most of the time businesses use a liquidation auction when they close a particular store or to open a new store. In these auctions, businesses mark down prices substantially to quickly clear out the inventory.