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Washington Enacts Earnest Money Disposition Process

The State of Washington has enacted legislation that is intended to resolve uncertainties surrounding the proper disposition of earnest money deposits held by title companies, escrow agents and real estate licensees when residential transactions fail to close.

Real estate transaction processes vary from jurisdiction to jurisdiction, and terms vary from contract to contract, but one of the most common elements among them is the earnest money deposit made by the buyer. The deposit establishes the buyer's commitment to undertake the necessary steps to close the transaction and also usually funds part of the mortgage down payment required by the lender. In transactions that do not close, however, disputes often arise regarding the disposition of the deposit. Or, even in the absence of a dispute, one of the parties may simply fail or refuse to cooperate with the execution of a written release authorizing the deposit holder to distribute the funds. As a result, earnest money holders face uncertainties regarding the proper disbursement of the funds, and may face legal liabilities for making the wrong decision. In some cases, the funds may remain in the holder's trust or escrow account indefinitely.

To address the problem, the Washington Department of Licensing/Washington Real Estate Commission organized a task force of stakeholders that included regulators, representatives of the state's escrow and title industries, the Northwest Regional Multiple Listing Service (NWMLS), the state REALTOR® association, and others. Washington REALTOR® and NWMLS representatives ably produce a draft bill upon which the task force reached a consensus. The resulting legislation, SHB 1730, has been enacted and will take effect on July 24, 2015.

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The new statutes provides that, if the earnest money "holder" (a real estate firm, title insurance company or agent, or escrow agent) in a residential real estate transaction involving improved or unimproved real property receives a written demand from a party to the transaction for all or a part of the earnest money, the holder must, within 15 days of receiving the demand, either notify all other parties of the demand, release the earnest money to one or more of the parties, or commence an interpleader action.

If the holder chooses the "demand and notice" option, the notice must include a copy of the demand and advise the other parties that they have 20 days to object; failing which the holder will release the money to the demanding party 10 days thereafter. The 20 day period begins on the date the notice is placed in the U.S. mail and the holder sends an email to the other parties, to the extent that such addresses have been provided and are contained in the holder's records for that transaction. The holder has no obligation to search outside its records for such addresses, and is not liable "for unsuccessfully locating the addresses" if outside records are used. The holder must, however, maintain a log or other method of evidencing the mailing of the notice.

If the holder receives a timely written objection or inconsistent demand from the other parties, the holder must within 60 days thereafter commence an interpleader action, unless both parties instruct the holder to either disburse the earnest money or delay commencement of the interpleader action for a specified period of time. [An interpleader action is a lawsuit in which the holder deposits the money in a court, which will decide its proper disposition and disbursement.]

In order to minimize the expense of an interpleader action, or even obviate the need to hire an attorney, SHB 1730 provides the forms that holders may use to issue interpleader summons and complaints, permits service of the documents by prepaid first class mail instead of personal service, and requires the deciding court to award the holder its reasonable attorney fees and costs.

The "demand and notice" process is not mandatory, and the earnest money holder can commence an interpleader action at any time. SHB 1730 protects holders from civil liability for either initiating the "demand and notice" process and/or commencing an interpleader action. That safe harbor from liability does not, however, protect an earnest money holder who, having received a written demand, does not employ either of those options and decides to release the funds to one or more of the parties.