

South Carolina Real Estate Trust Account Guidelines



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REAL ESTATE TRUST ACCOUNTS

Introduction

The primary purpose of the South Carolina Real Estate License Law and Regulations is to protect the public. The purpose of the South Carolina Real Estate Commission is to administer and enforce those laws and regulations. It is the objective of the Commission to render the highest possible level of service to all licensees while protecting the rights of citizens of South Carolina.

The Commission has responsibility for periodically inspecting trust account records of real estate and property management offices in the state of South Carolina. During these inspections, the Commission emphasizes the fiduciary duty of the real estate licensees when they enter into an agency relationship with a principal. One of the most important duties is accounting for funds entrusted to the licensee.

This booklet is intended to inform real estate licensees about the Commission's interpretation of the law concerning accounting requirements necessitated by each licensee's duties. It also offers instruction on proper procedures. Lack of knowledge in proper escrow accounting procedures often results in complaints against licensees, financial loss to consumers, and disciplinary action by the Commission.

The Real Estate Commission has vested special authority in any individual licensed as a broker-in-charge or property manager-in-charge. These persons are empowered to act as trustees of funds belonging to others being held pending the consummation or either termination of a real estate transaction. Along with that authority goes the responsibility for proper accounting, which cannot be delegated. The employment of a professional service or trained staff member to keep the records will not relieve the licensee of legal responsibility, or properly supervising, training, and reviewing the work of the employees performing this important function. As an example, a simple oversight could result in an NSF (non-sufficient funds) check being issued against the trust account. In addition to the embarrassment, bank charges and added accounting required to correct the problem, an NSF check written on a trust account is considered prima facie evidence of "untrustworthiness or incompetency in such a manner as to endanger the interest of the public," and may result in disciplinary action. Proper recordkeeping and accounting are imperative in the establishment and maintenance of the trust account.

Contained within this booklet are sections of the Real Estate License Law that pertain to the management of a trust account, definitions, and the view of the Commission regarding trust account management. While no single treatment of this subject can answer all questions or address all situations a licensee may encounter, this booklet is intended to deal with the most frequently asked questions and those situations most often experienced during a "typical" real estate transaction.

The instructions are designed as a tool to assist the licensees. The methods and forms are provided as suggestions only and should not be viewed as the only way to manage a trust account. There are many good computer software packages in the market that can make maintaining a trust account easy while providing fail-safe mechanisms to prevent errors. Remember, however, that adequate backup must also be maintained in a separate location. These recommendations should be viewed as supplementary to the fundamentals of sound accounting procedures in the real estate industry.

Please read this booklet in its entirety and call the Commission with any questions.

Acknowledgements

Special thanks go to the following for their volunteer effort in updating this trust account booklet:

South Carolina Real Estate Commission Members 2018-2019

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GENERAL INFORMATION

The requirement to establish and maintain a real estate trust account pertains to each individual licensed as a broker-in-charge (BIC) or property manager-in-charge (PMIC) who holds the funds of others.

Trust funds are funds received by a licensee on behalf of another person in the course of performing any real estate activity. These funds do not belong to the licensee but are being held for the benefit of others. A “trust account” is simply a bank account into which trust funds (and only trust funds) are deposited. It must be separate from a business or personal account and must provide for withdrawal of the funds.

By depositing trust funds in a designated trust account and keeping accurate records that identify each depositor, the funds are protected from being “frozen” or attached by lienholders should the licensee become involved in legal action, become incapacitated or die. Furthermore, by placing these funds in a separate account, licensees are less likely to confuse the trust funds with personal or business funds and inadvertently use monies belonging to others for personal or business purposes.

- 1. Commingling Trust Funds** – This term is defined as mixing the licensee’s funds with those held in trust for another. Personal funds may not be placed in the trust account. The licensee may open the account with business or personal funds and is permitted to maintain a minimum of personal funds in order to keep the account active. Funds in a trust account later becoming funds of the licensee should be removed immediately. For example, when commissions are due from monies held in a trust account, they must be transferred to a corporation or company account before disbursement.
- 2. Conversion of Trust Funds** – Conversion occurs when trust funds are used for any purpose other than that for which they are held. This might involve a licensee converting the funds for personal or business use, or it might involve using one client’s funds for the benefit of another client and is a criminal act.

BASIC REQUIREMENTS THE TRUST ACCOUNT MUST MEET

As previously stated, the procedures outlined in this booklet are not the only method that can be used to maintain a trust account. However, regardless of which method is used, the account records must provide an adequate audit train. The basic requirements for South Carolina trust accounts are to:

1. Include all information required by South Carolina Real Estate License Law.
2. Identify **exact** amount in the account at **all** times.
3. Identify ownership of funds in the account, by amount, at all times.
4. Provide a consistent and logical record of the account.

DEFINITIONS

COMMINGLING: To mingle or mix; for example, to deposit in the licensee's personal or general business account funds held in trust.

COMMISSION: An agent's compensation for the performance of the duties of the agency.

CONVERSION: The process of changing or causing something to change from one form to another.

DEPOSITABLE TRUST ITEMS: Funds (cash, checks, money orders, bank drafts) acceptable for deposit in a bank that are received by the licensee for the benefit of others.

EARNEST MONEY: Payment made by a prospective purchaser of real estate as evidence of good faith.

FOLIO NUMBER: An internal or sub-account number created by the individual maintaining the trust account records – used to numerically identify separate accounting for individual transactions.

GENERAL LEDGER (JOURNAL): A chronological record of funds that are received and disbursed.

NON-DEPOSITABLE TRUST ITEMS: Any instrument or equity or thing of value not acceptable for deposit in a bank that is received in lieu of monies by the licensee for the benefit of others.

OWNER'S LEDGER: A sub-account record that identifies funds received from, or disbursed to, a particular owner of property being managed.

RECONCILIATION OF TRUST ACCOUNT: A periodic process (usually monthly) whereby the account balance shown on a bank statement is compared to and balanced with the general ledger, the sub-ledger, and the checkbook balances.

SECURITY DEPOSIT: Money deposited by or for a tenant with the licensee that is placed in trust. The landlord may claim, under certain circumstances, portions of a security deposit to offset damages caused by the tenant or nonpayment of rent as provided by law. (See SC Residential Landlord/Tenant Act of 1986 for more details.)

SUBSIDIARY LEDGER: An excerpt from the general ledger pertaining only to the funds belonging to one particular individual, property, or transaction.

TENANT’S LEDGER: A sub-account record that identifies funds received from, or disbursed to, a particular tenant.

TRUST ACCOUNT: An account separate and apart and physically segregated from licensee’s own funds, in which the licensee is required, by law, to deposit all funds collected on behalf of clients or other parties.

TRUST FUNDS: Money or other items of value not belonging to but received by the licensee on behalf of others.

TRUSTEE: The person to whom funds are entrusted upon certain terms and conditions for the benefit of another.

Note: Although “trust account” and “escrow account” are used interchangeably in practice, the term “trust account” will be used in this booklet.

CHAPTER 1

THE SOUTH CAROLINA REAL ESTATE LICENSE LAW

The South Carolina Real Estate License Law and Regulations are located under Chapter 57, Title 40, *Code of Laws of South Carolina, 1976 as amended*. The following are excerpts from the License Law that pertain to the establishment and maintenance of real estate trust accounts:

Section 40-57-135. (A) A broker-in-charge or property manager-in-charge shall:

(1) adequately supervise employees or associated licensees to ensure their compliance with this chapter;

(3) maintain adequate, reasonable, and regular contact with associated licensees engaged in real estate transactions so as to prevent or curtail practices by a licensee which would violate any provision of this chapter, Chapter 1, Title 40, the Interstate Land Sales Practices Act, or the Vacation Time Sharing Plans Act;

(7) establish and maintain control of and responsibility for an active trust account when in possession of trust funds belonging to others resulting from a real estate transaction; and

(8) notify the commission by mail within ten days of any change of office name, address, email address, or telephone number

Section 40-57-136. (A)(1) A broker-in-charge or a property manager-in-charge, when taking possession of trust funds, shall establish and maintain control of and responsibility for an active real estate trust account which must be a demand deposit account designated and titled to include the word 'trust' or the word 'escrow' in the name of the real estate brokerage firm for which the respective broker-in-charge's or property manager-in-charge's license is issued; provided, however that one central trust account may be used by real estate brokerage firms with multiple offices managed by:

(a) one broker-in-charge or one property manager-in-charge; and

(b) separate brokers-in-charge or separate property managers-in-charge.

(2) A broker-in-charge and a property manager-in-charge shall maintain records which reflect the transactions in his office.

(3) A trust account maintained by a broker-in-charge or property manager-in-charge must be a demand deposit account located in an insured financial institution authorized to conduct business in South Carolina.

(4) A broker-in-charge or property manager-in-charge shall instruct employees and associated licensees on the proper handling of trust funds.

(5) A check or statement issued in connection with a real estate trust account must reflect the title and designation of the account as provided in item (1).

(B)(1) A broker-in-charge or property manager-in-charge shall ensure that accurate and complete records, as required by this chapter, are maintained for real estate trust accounts.

(2) A broker-in-charge or property manager-in-charge shall ensure that backup copies are maintained for computerized real estate trust accounts. A backup copy must be maintained on a data storage medium that is stored in a separate off-site location.

(3) A broker-in-charge or property manager-in-charge may not commingle trust funds of the client with his own money, except that he may maintain a clearly identified amount of the company's funds in the trust account to cover bank service charges or in order to avoid the closing of the account when no client's trust funds are on deposit.

(4) Trust funds received by a licensee in connection with a real estate transaction in which the licensee is engaged for the broker-in-charge or property manager-in-charge must be delivered to the broker-in-charge or property manager-in-charge no later than the following business day.

(5) A broker-in-charge or property manager-in-charge who disburses trust funds contrary to the terms of the contract or fails to disburse trust funds not in dispute is considered to have demonstrated incompetence to act as a broker-in-charge or property manager-in-charge.

(C)(1)(a) Except as provided in sub-item (b), trust funds received by a broker-in-charge or property manager-in-charge in a real estate rental or lease transaction must be deposited as follows in a real estate trust account as follows:

(i) cash or certified funds must be deposited within forty-eight hours of receipt, excluding Saturday, Sunday, and bank holidays; and

(ii) checks must be deposited within forty-eight hours after a lease or rental agreement is signed by the parties to the transaction, excluding Saturday, Sunday, and bank holidays.

(b) Rent received by a licensee who is directly employed by the owner of rental property may be deposited in an operating or other similar account, but otherwise must be properly accounted for as provided in this section. However, an advance rental deposit is a trust fund and must be treated as such.

(2) Trust funds received by a broker-in-charge or property manager-in-charge in connection with a real estate rental or lease including, but not limited to, security deposits, pet deposits, damage deposits, and advance rentals, except earned rental proceeds, and deposited in the trust account must remain in the trust account until the lease or rental transaction expires or is terminated, at which time undisputed trust funds must be disbursed pursuant to the contract which directs the broker-in-charge or property manager-in-charge to hold the trust funds, and a full accounting must be made to the landlord or tenant as appropriate. Earned rental proceeds must be disbursed to the landlord within a reasonable time after clearance of the deposit by the bank.

(D)(1)(a) Trust funds received by a broker-in-charge in a real estate sales or exchange transaction must be deposited as follows in a separate real estate trust account:

(i) cash or certified funds must be deposited within forty-eight hours of receipt, excluding Saturday, Sunday, and bank holidays;

(ii) checks must be deposited within forty-eight hours after written acceptance of an offer by the parties to the transaction, excluding Saturday, Sunday, and bank holidays;

(b) Trust funds received by a broker-in-charge in connection with a real estate sales or exchange transaction and deposited in the real estate trust account shall remain in the trust account until consummation or termination of the transaction, at which time the undisputed trust funds must be disbursed in accordance with the contract which directs the broker-in-charge to hold the trust funds, and a full accounting must be made to the parties.

(2) A broker-in-charge or property manager-in-charge who disburses trust funds from a designated trust account under the following circumstances is considered to have properly fulfilled the duty to the account:

(a) upon rejection of an offer to buy, sell, rent, lease, exchange, or option real estate;

(b) upon the withdrawal of an offer not yet accepted by the offeree; or

(c) at the closing of the transaction.

(E) If a dispute concerning the entitlement to, and disposition of, trust funds arises between a buyer and a seller, and the dispute is not resolved by reasonable interpretation of the contract by the parties to the contract, the deposit must be held in the trust account until the dispute is resolved by:

(1) a written agreement which:

(a) directs the disposition of monies signed by all parties claiming an interest in the trust monies, and

(b) must be separate from the contract which directs the broker-in-charge or property manager-in-charge to hold the monies;

(2) filing an interpleader action in a court of competent jurisdiction;

(3) an order of a court of competent jurisdiction; or

(4) voluntary mediation.

(F)(1) Records required by this chapter must be maintained for a minimum of five years and the broker-in-charge or property manager-in-charge shall furnish a copy of the records to a representative of the commission upon request. Accounting records that may be requested include, but are not limited to, journals, ledgers, folios, client subaccounts, tenant accounts, canceled checks, deposit slips, and bank statements.

(2) Brokers-in-charge or property managers-in-charge, when required by this chapter to establish and maintain a real estate trust account, also shall maintain, in their designated principal place of business, a recordkeeping system consisting of:

(a) a journal or an accounting system that records the chronological sequence in which funds are received and disbursed for real estate sales. For funds received, the journal or accounting system must include the date of receipt, the name of the party from whom the money was received, the name of the principal, identification of the property, the date of deposit, the depository, the payee, and the check numbers, dates, and amounts. A running balance must be maintained for each entry of a receipt or disbursement. The journal or accounting system must provide a means of reconciling the accounts;

(b) a journal or an accounting system containing, for property management, the same information as stated in sub-item (a) except that the required running balance may be determined at the time of reconciliation;

(c) a separate record for each tenant identifying the unit, the unit owner, amount of rent, due date, security deposit, and all receipts with dates when managing property. An owner's ledger also must be maintained for all properties owned by each owner showing receipts and disbursements applicable to each property managed. A disbursement must be documented by a bid, contract, invoice, or other appropriate written memoranda;

(d) a trust account deposit document must identify the buyer or tenant unless other appropriate written memoranda are maintained;

(e) a general ledger identifying security deposits;

(f) a monthly reconciliation of each separate account except when no deposit or disbursement is made during that month. The reconciliation must include a written worksheet comparing the reconciled bank balance with the journal balance and with the ledger total to ensure agreement.

(G) Trust funds received by a broker-in-charge or property manager-in-charge which must be deposited in a trust account may be deposited in an interest-bearing account. Interest earned on these trust funds may be retained by the broker-in-charge or property manager-in-charge if:

(1) the depositors or owners of the trust funds have been informed of their right to ownership of the interest but relinquish the right of ownership to the broker-in-charge or property manager-in-charge by written agreement; and

(2) the agreement, if part of a preprinted form, uses conspicuous language.

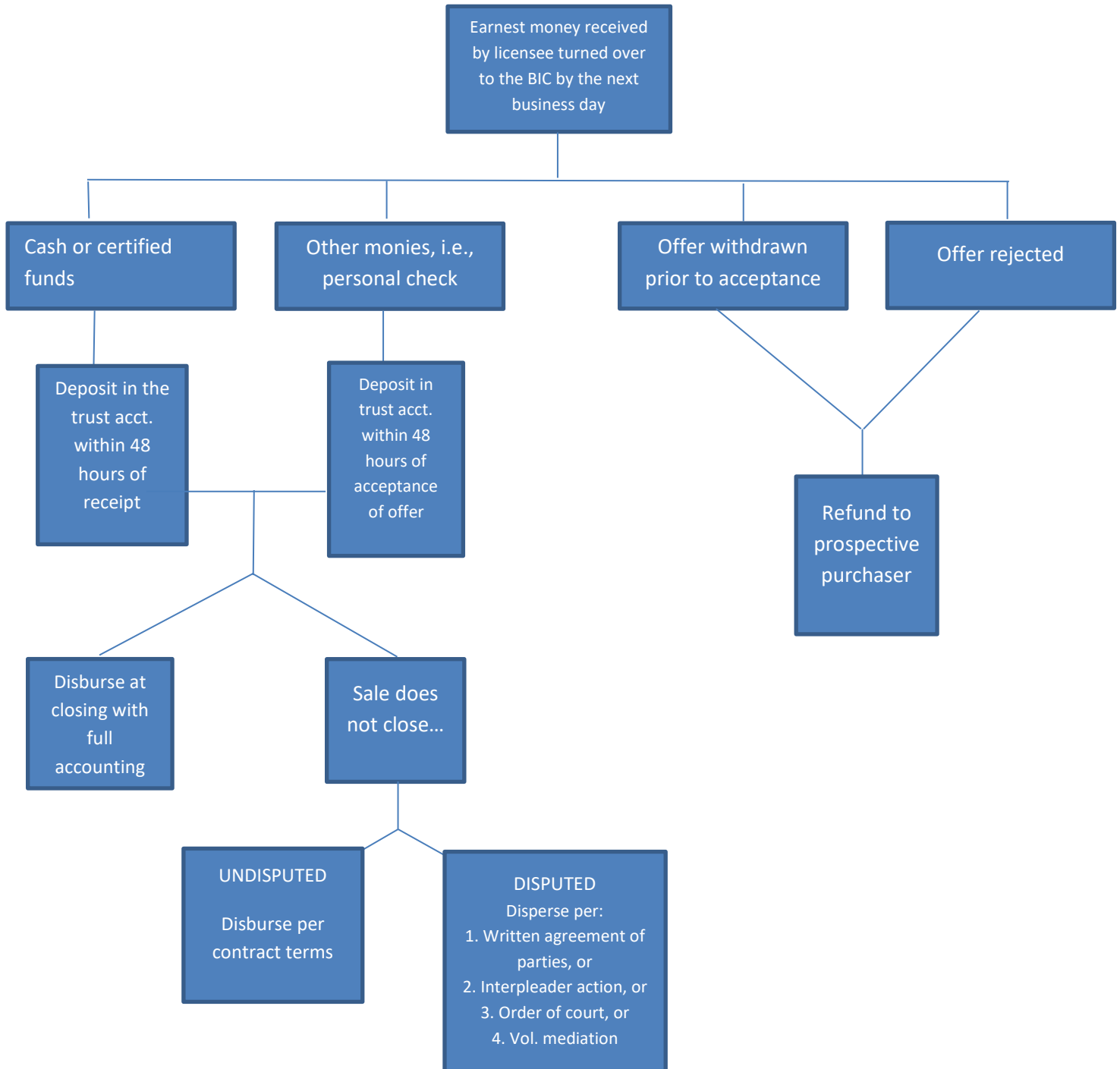
40-57-145 GROUNDS FOR DISCIPLINARY ACTION. – (A) In addition to Section 40-1-110, the Commission may deny issuance of a license to an applicant or may take disciplinary action against a licensee who:

(10) fails, within a reasonable time, to account for or remit any monies coming into his possession which belong to others;

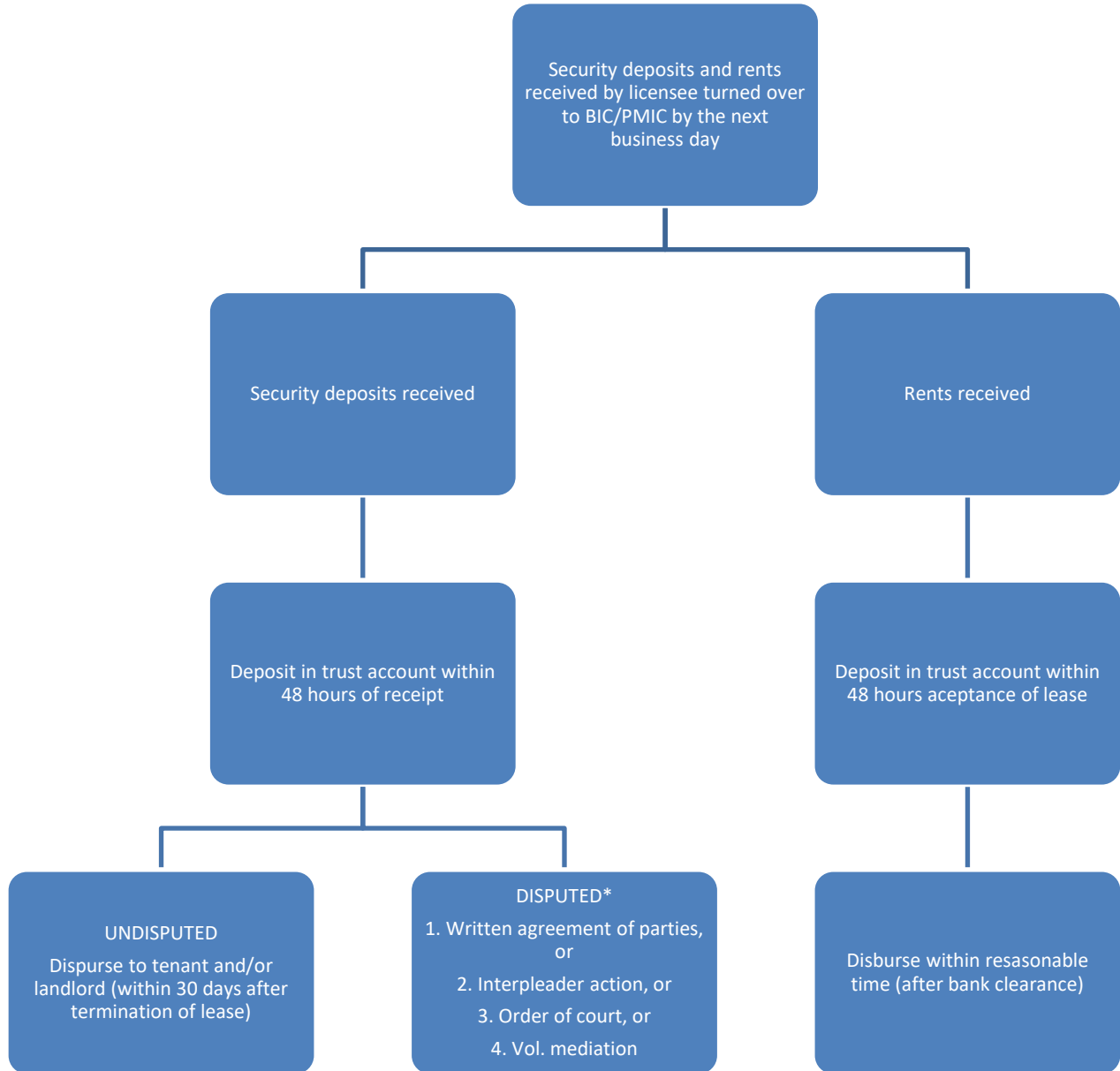
(17) accepts deposit money which is to be delivered to the licensee's principal in a real estate transaction without informing the payor and having the payor acknowledge in writing who shall hold the money received by the licensee;

(18) issues a check in connection with the real estate business which is returned for insufficient funds or closed account.

HANDLING OF TRUST FUNDS FOR REAL ESTATE SALES



HANDLING OF TRUST FUNDS FOR PROPERTY MANAGEMENT



*Although the law refers to earnest money disputes only, the Commission recommends the same course of action for disputed security deposits.

CHAPTER 2

GENERAL COMMENTS ABOUT THE LAW

In the preceding chapter, excerpts from the South Carolina Real Estate License Law were included for your information. Since laws can sometimes be difficult to interpret, this chapter is dedicated to simplifying their intent into language that can be more easily understood.

1. Licensees receiving trust funds from buyers, sellers, or tenants must turn them over to their BIC or PMIC by the next business day.
2. All monies received by the BIC/PMIC on behalf of a principal in a real estate transaction must be placed in a bank account specifically designated “escrow” or “trust” account. These funds will be properly accounted for until such time as all funds are disbursed at the consummation or other termination of the transaction.
3. BICs/PMICs should maintain a numbered duplicate receipt system, one for the payor and one for the file, accounting for all monies received and posted to a cash receipts journal. All monies received shall be identified by the date received and by the amount, source, and purpose. Receipt numbers should be recorded in the general ledger and kept on file for a period of five years. Checks issued from a trust account must be sequentially pre-numbered, bear the name of the firm (as licensed), and be identified as a real estate trust account.
4. Trust account records must be maintained to allow an easy analysis of the sources and uses of funds. An investigator should be able to enter a BIC’s/PMIC’s office, examine the trust account records, and see where, when, to whom, and for what purpose funds have been received and disbursed, along with all necessary authorizations and source documents.
5. Paper trails are properly provided if the minimum trust account requirements mandated by the License Law are followed. Remember to post all required information on checks, check stubs, and deposit slips.
6. When a BIC/PMIC receives funds that are immediately negotiable (cash, certified funds), they should be deposited into the trust account within 48 hours of receipt (excluding Saturdays, Sundays, and bank holidays). If funds are in the form of personal or company checks, they should be deposited within 48 hours (excluding Saturdays, Sundays, and bank holidays) after acceptance of an offer or the signing of a lease.

7. Once a BIC/PMIC deposits funds into the trust account, those funds may not be removed from the account for any reason until consummation or other termination of the real estate transaction. A full accounting is then to be provided by the BIC/PMIC to the trustor.

8. Rental payments are processed through the trust account just as any other escrow funds and then disbursed in accordance with the management agreement. The only exception to this is where the licensee is a direct employee of the owner. In these cases, rent monies are not required by law to be placed into an escrow account. Disbursement of rental payments can be made upon receipt of cash, certified check, or when a personal check has cleared the bank, as a payment of rent constitutes consummation of that portion of the lease. However, security deposits must remain in the trust account until termination of the lease.

CHAPTER 3

REQUIRED RECORDS

The BIC/PMIC is required to set up an accounting system that consists of the following records:

FOR ALL TRANSACTIONS (SALES AND PROPERTY MANAGEMENT)

1. GENERAL LEDGER OR JOURNAL: These two terms are interchangeable, but in this booklet, the term “general ledger” is used. The general ledger is a recording of all funds coming into and going out of the trust account in the chronological sequence in which the events occur. The general ledger shall contain the following headings:

1. Date of transaction (check written or deposit made)
2. Deposit or check number
3. Payor (buyer or seller for sales, landlord or tenant for property management)
4. Principal (client)
5. Property address
6. Payee
7. Folio number
8. Check amount
9. Deposit amount
10. Balance in account
11. Remarks

2. SUBSIDIARY ACCOUNT LEDGERS: In addition to the general ledger, the law requires a separate record be maintained for each individual’s money being held in the trust account. This is accomplished by establishing separate sub-account ledgers, one for each transaction for which the BIC/PMIC is holding money. This “mini” version of the general ledger pertains only to the deposits and disbursements involved with a particular principal or trustor. Since the total of all the money within a trust account at any given time usually belongs to several individuals, a separate accounting for each individual is required. This enables someone to determine the owner of all funds held in the trust account. The total of the sub-accounts should equal the running balance recorded in the general ledger and checkbook at all times. Any personal or company funds must also be reflected in a sub-account ledger. One of the most frequent mistakes made in trust account records is the failure to establish the sub-account for BIC/PMIC company/personal funds. Without that particular sub-account, the total of sub-accounts can never equal the general ledger and checkbook balances and the trust account would not be reconcilable.

3. THE CHECKBOOK: A record of all deposits and disbursements must be entered into the trust account checkbook. The checkbook balance, therefore, must **always** equal the total of the sub-accounts as well as the balance on the general ledger.

4. THE BANK STATEMENT: Normally the bank will issue a monthly statement of the account that will show the balance the banker collects on a given date. That balance may not agree with other records because some of the other checks may remain outstanding (may not have cleared the bank), and some of the deposits may not have been credited to the account at the time the bank issued the statement.

Reconciling is accomplished by identifying which checks and/or deposits were outstanding at the time the bank issued its statement. These must be subtracted or added, respectively, from the balance shown on the bank statement. Usually the bank statement will list checks in numerical sequence and deposits by date, so that items that are absent from the bank statement may be easily identified when comparing to the checkbook. Once all “outstanding” checks have been subtracted from, and all “outstanding” deposits are added to the bank statement balance, then the bank statement is reconciled and both balances should agree. If they do not, the arithmetic should be checked. The worksheet used in reconciling (usually found on the reverse side of the bank statement) must be retained with the records and is subject to inspection by the Commission. This is the first step in reconciling a trust account.

5. SALES CONTRACTS AND/OR LEASES: Each deposit into the trust account must be supported by a contract that states the exact amount to be held by the BIC/PMIC. The trust account records should reflect the contract amount as being held in the bank for a particular transaction. Therefore, the total stated on all open contracts, plus any company/personal funds in the account, must always equal the general ledger running balance, the total of all the sub-accounts, and the checkbook balance.

6. RECEIPTS AND DEPOSIT SLIPS: All receipts and deposits slips verifying disbursements and deposits involving the trust account must be kept for a period of five years. The receipt and deposit system should be numbered, or organized in some other logical sequential format, to allow for complete accountability.

7. PERSONAL FUNDS: It is permissible for the BIC/PMIC to place personal or company funds into the trust account if they are clearly identified. The reason for allowing personal funds in the account is to defray bank service charges and to avoid account closure by the bank when no client monies are on hand. A sub-account for BIC/PMIC personal/company funds must, therefore, be established and maintained to keep those funds clearly identified. Any amount over the minimum requirement of the bank could be considered excessive and could place the BIC/PMIC in a “commingling” situation. Bank service charges, check printing charges, and other related expenses should be deducted from the personal funds sub-account. Also, such charges should be deducted from the general ledger and checkbook balances when they occur.

8. FOLIO NUMBERS: A folio number is an account/sub-account number assigned by the individual maintaining the trust account records for internal purposes only. A separate folio number is assigned to each new sub-account that is established, and the same folio number is indicated in the general ledger for each entry. This creates a method of tracking individual transactions in the general ledger by number as well as by name. There is no specific system that must be used when assigning folio numbers, as long as it is logical and consistent. The Real Estate License Law does not require the use of folio numbers, but it is a highly recommended accounting principle.

9. INTEREST: 40-57-136 (G) allows trust funds to be placed in an interest-bearing account. Any accrued interest belongs to the owners of the funds unless they agree otherwise in writing. If the owners of the funds do not relinquish their right to the interest, and interest is earned, it must be posted to each respective sub-account, the general ledger, and the checkbook balance. If the right to interest is relinquished, due care must be taken to withdraw that money from the trust account periodically to preclude BIC/PMIC personal/company funds escalating into a “commingling” situation.

FOR PROPERTY MANAGEMENT TRANSACTIONS

1. REQUIREMENTS: BICs/PMICs engaged in property management are required to keep records as described for all transactions on the preceding pages with the following differences.

A. Sec 40-57-136 (f) (2) (b) states for property management: "...the required running balance may be determined at the time of the reconciliation." A new balance need not be shown after each entry in the general ledger but must be shown periodically when all the sub-accounts and the bank statement are reconciled with the general ledger and check balances (usually monthly).

B. Two sub-accounts must be maintained for each transaction – a tenant's ledger and an owner's ledger. The following information must be recorded as a part of the heading for each ledger:

1. Identification of the unit or property (address);
2. The unit and property owner (tenant and owner);
3. The amount of rent (each payment);
4. The due date of the rent; and
5. The amount of security deposit held.

As a part of the tenant's ledger, there should also be entries of the date and amount of each receipt for or on behalf of the tenant.

As a part of the owner's ledger, there should also be:

1. Any and all receipts applicable to the property;
2. The disbursements for expenses on the property documented by bids, contracts, or invoices (invoices furnished to owners should be numbered to avoid confusion);
3. The disbursement of rental proceeds to the owner and commission to the BIC/PMIC.

A periodic reconciliation of the tenant's and owner's ledgers (sub-accounts) is required and must balance with the bank statement, checkbook, and general ledger. The major difference between sales and property management accounting is that when the bank issues its monthly statement on the account, there may have been rental proceeds in the account not yet disbursed to the owner which must be taken into consideration when reconciling the bank statement. Any repairs or other expenses must be accurately annotated on the owner's ledger (sub-account) in order to balance the account to the general ledgers.

NOTE: The law does allow both property management and sales funds to be maintained in the same trust account, but if they are, the requirement of entering a running balance after each entry (required for sales accounting) would take precedence. This would be extremely cumbersome for property management, and for that reason, the Real Estate Commission recommends establishment and maintenance of separate trust accounts for sales and property management.

NOTE: 40-57-136 (F) (1) requires records to be held for a minimum of five years and every broker or property manager must voluntarily furnish a copy of said records to a representative of the South Carolina Real Estate Commission upon request.

CHAPTER 4

RECONCILING BANK STATEMENTS WITH TRUST ACCOUNT RECORDS

Reconciling the bank account is only the first step in reconciling the total trust account record. A mandatory worksheet is required for monthly trust account reconciliation. And remember, these worksheets are subject to inspection by the Real Estate Commission and must be kept for a period of five years. A sample reconciliation form is shown below.

Simplified 4-way crosscheck

Identify contracts with outstanding earnest money deposits, leases with security or other deposits, other outstanding trust items, and BIC funds in trust account

Earnest money deposits from open contracts _____

Security or other deposits from leases _____

BIC personal funds _____

1. Total open trust funds from above _____

2. What is checkbook balance? _____

3. What is general ledger balance? _____

4. Total subaccount ledger balances _____

Are all four totals the same? Yes or No

If no, explain.

CHAPTER 5

ACTIONS TO BE AVOIDED

1. Never pay your license renewal fee, agent's renewal fees, change of name or address fees, or any other fees charged by the Real Estate Commission from a trust account.
2. Never disburse trust funds when there is a dispute about their disposition between buyer and seller or tenant and owner. Disputed trust funds must remain in your account until the dispute is settled by one of the four actions listed previously.
3. Never leave a commission in the trust account after the transaction has closed.
4. Never close your business and trust account before you turn in your license to the Real Estate Commission, unless you are authorized in advance to do so by the Commission.
5. Never invest trust funds in any type of interest-bearing securities or certificate accounts. The trust account must be a demand account in an insured financial institution.

CHAPTER 6

FREQUENTLY ASKED QUESTIONS ABOUT TRUST ACCOUNTS

Q. Do rents collected go into the trust account?

A. Yes. All monies belonging to others collected in real estate transactions must be deposited into the trust account. Payments to the owner for rent and to the BIC/PMIC for the commission are disbursed from the trust account. A full accounting of the rental payment must be shown in records kept by the licensee. The only exception to this rule is where the BIC/PMIC is employed by the owner. In these situations, the rents may be deposited into an operating account.

Q. I disburse rents to the owner immediately. Why should I deposit rent collected into the trust account?

A. There are several reasons. If the rent payment check is deposited into the business or operating account, it would amount to commingling of funds, which is prohibited by law. If the payment is made in cash, it must be deposited so that proper accounting can be shown in the BIC/PMIC trust account records. Although the money may have been received and disbursed the same day, it is still money being held for another and must be handled through the trust account to provide full accountability. It is advisable to wait until a check clears before disbursing proceeds.

Q. Can I have more than one trust account?

A. Yes. Many brokers maintain separate trust accounts for sales and rental transactions. This is not only acceptable but is recommended provided each account is designated as a "trust" or "escrow" account.

Q. Why is a trust account necessary?

A. The law requires it to protect the public. The audit of the account will help ensure that BICs/PMICs are not misusing money belonging to others in violation of the South Carolina Real Estate License Law.

Q. Can I leave my commission in the trust account for a period of time after I have closed out the transaction?

A. No. All funds must be expended at the time of closing. You are allowed to keep only a small amount of personal funds in the trust account to avoid bank service charges and/or to keep the account from being closed by the bank when no trust funds are on deposit. Any additional amount, such as earnest commissions, may be considered commingling.

Q. Our company deposits all earnest money in a trust account; however, at closing, the earnest money is withdrawn and placed into the office operating account along with the final settlement money. All disbursements are then made from the office operating account. Is our company in violation of the law?

A. Yes. All transactions involving trust funds must be processed through and accounted for in the trust account. Earnest money and settlement money may not be disbursed (totally or in part) until the time of closing or termination of the contract. If an attorney is handling the closing, the earnest money may be disbursed to that attorney's trust account prior to closing to be included with the settlement money disbursed by that attorney. Another acceptable procedure is that the attorney may credit the earnest money on the closing statement and the BIC will then disburse to the operating account and apply that amount as part of the earned commission.

Q. I have an active BIC/PMIC license, but I'm not really active in the real estate business. Do I still have to maintain a trust account?

A. A trust account is only required if you are holding the funds of others.

Q. Can I, as a BIC/PMIC, draw the interest earned on money that I am holding in my trust account?

A. It is possible provided you meet all the conditions listed in License Law. Once interest is earned, however, it becomes earned income of the BIC/PMIC and must be disbursed out of the trust account or you may be commingling funds.

Q. The deal fell through and the buyer and seller are in dispute over who should get the earnest money. What do I do?

A. In this situation, License Law directs a broker to hold the earnest money in the trust account until such a time as its disposition is determined. The broker may attempt to bring the parties to agreement, and/or advise them of the four options, including the court system.

Q. I have my account set up to read "Special Account." Is that all right?

A. No. The account title must read either "Escrow" or "Trust." No other terminology is acceptable.

Q. I am the selling broker and the contract calls for the listing broker to hold the earnest money, but the prospective purchaser wrote the check and gave it to me. What do I do?

A. There is a difference between "coming into receipt" of funds and "accepting" funds. If the check is made out to the selling broker in this case, and the selling broker takes possession of the check, the selling broker is said to be in "receipt" of the funds. In this particular situation, a new check should be issued by the prospective purchaser and made payable to the listing broker unless otherwise specified in the contract. However, if the check is already made out to the listing broker and given to the selling broker to deliver, then the selling broker is only "accepting" funds and must deliver them to the listing

broker in a timely manner. The selling broker is not obligated in that instance to place the funds into his or her own trust account.

Q. Is there anything improper about my “borrowing” a small sum from the trust account for my regular business expenses as long as it is paid back before it is due to my client?

A. Yes. This is the most serious violation a BIC/PMIC can commit. Not only would it be conversion or misappropriating trust funds for personal use, but it could also place the BIC/PMIC in a breach of trust situation where criminal charges could be brought against the BIC/PMIC as well as subjecting the licensee to discipline.

Q. What happens if a BIC/PMIC is unable to account for all funds belonging in the trust account?

A. The Real Estate Commission could direct the issuance of charges against the licensee and hold a hearing before the Commission to determine whether sufficient information exists to take disciplinary action. The Commission may revoke or suspend the individual’s license and could place restrictions on the licensee, as well as a monetary fine.

Q. When the Real Estate Commission audits my real estate trust account, what records will I be asked to furnish?

A. The investigator could require all of the following:

- General ledger
- All sub-ledgers
- All agency representation agreements
- All management agreements
- Checkbook and bank statements
- All sales contracts
- All leases and options
- All closing statements
- All other related documents

The above records must be held for a minimum of five years.

Best Practices

When Attorney Holds Earnest Money

If lawyers are responsible for the money or property of clients of third parties, they are governed by Rule 1.15 of the Rules of Professional Conduct, which addresses the safekeeping of the money and property, and South Carolina Appellate Court Rule 417, which addresses the required record keeping. The basic rules of trust accounting—no commingling, no conversion, good recordkeeping, record retention and timely reconciliations—are very similar to Real Estate License Law.*

Real estate customers and clients often ask if the lawyer can accept a personal or business check rather than a wire or certified check. Rule 1.15 provides that a lawyer cannot disburse funds “unless the funds to be disbursed have been deposited in the account and are collected funds; provided, however, a lawyer may treat as equivalent to collected funds....”* The basic rule is that a lawyer cannot disburse the funds at closing unless the funds have cleared the bank.

Without the exception of certain funds being the “equivalent” funds that have cleared the bank, closings would be much harder to fund. Funds included in this exception are “cash, properly endorsed government checks, certified checks, cashier’s checks” and other checks that do not exceed \$5,000 if “the lawyer has reasonable and prudent belief that the deposit of such other instrument will be collected promptly.”

In other words, lawyers can disburse funds from personal or business checks that do not exceed \$5,000 if the lawyers reasonably believe the check will not bounce. However, if the check does bounce, lawyers must deposit funds to cover it “as soon as practical but in no event more than five working days after notice of non-collection....” Lawyers are under the additional requirement that they must give the bank a “written directive requiring the institution to report to the Commission on Lawyer Conduct when payment is returned for insufficient funds.”* This ensures that the Supreme Court is aware of the issue and can take appropriate disciplinary measures.

Unlike the four specific ways to disburse disputed funds in Real Estate License Law, the rule governing lawyers is much more general: “When in the course of representation a lawyer is in possession of property in which two or more persons (one of whom may be the lawyer) claim interests, the property shall be kept separate by the lawyer until the dispute is resolved....”* Consequently, many lawyers require the parties to sign a separate Escrow Agreement that defines how any disputes will be resolved.

¹ Rule 1.15(a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property. Funds shall be kept in a separate account maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third person. Other property shall be identified as such and appropriately safeguarded. Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of six years after termination of the representation. A lawyer shall comply with Rule 417, SCACR (Financial Recordkeeping).

² Rule 1.15(f) A lawyer shall not disburse funds from an account containing the funds of more than one client or third person unless the funds to be disbursed have been deposited in the account and are collected funds; provided, however, a lawyer may treat as equivalent to collected funds cash, verified and documented electronic fund transfers, or other deposits treated by the depository bank as equivalent to cash, properly endorsed government checks, certified checks, cashier's checks or other checks drawn by a bank, and any other instrument payable at or through a bank, if the amount of such other instrument does not exceed \$5,000 and the lawyer has reasonable and prudent belief that the deposit of such other instrument will be collected promptly. If the actual collection of deposits treated as the equivalent of collected funds does not occur, the lawyer shall, as soon as practical but in no event more than five working days after notice of noncollection, deposit replacement funds in the account.

³ Rule 1.15(h) Every lawyer maintaining a law office trust account shall file with the financial institution a written directive requiring the institution to report to the Commission on Lawyer Conduct³ Rule 1.15(a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property. Funds shall be kept in a separate account maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third person. Other property shall be identified as such and appropriately safeguarded. Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of six years after termination of the representation. A lawyer shall comply with Rule 417, SCACR (Financial Recordkeeping).

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³ Rule 1.15(h) Every lawyer maintaining a law office trust account shall file with the financial institution a written directive requiring the institution to report to the Commission on Lawyer Conduct when any properly payable instrument drawn on the account is presented for payment against insufficient funds. No law office trust account shall be maintained in a financial institution that does not agree to make such reports. The inadvertent failure of the institution to provide the report required by this rule shall not be construed to establish a breach of duty of care, or contract with, the Court or any third party who may sustain a loss as a result of an overdraft of a lawyer trust account.

⁴Rule 1.15(e) When in the course of representation a lawyer is in possession of property in which two or more persons (one of whom may be the lawyer) claim interests, the property shall be kept separate by the lawyer until the dispute is resolved. The lawyer shall promptly distribute all portions of the property as to which the interests are not in dispute.

Sample Language for Attorney Escrow Agreement

The escrow agreement will state the law firm will hold the buyer's earnest money of \$ _____ in the lawyer's trust account and will be disbursed to the closing as a buyer credit on the settlement statement in a timely/proper transaction closing but if the transaction fails to timely/properly close then the money will be disbursed as follows: \$ _____ to buyers and \$ _____ to sellers and \$ _____ to broker(s) _____ on the _____ days after the failed closing date unless the seller or buyer have served a properly filed lawsuit on the earnest money to the lawyer holding the money in trust whereupon the lawyer will hold the money indefinitely until receiving a disbursement document signed by all the buyers and sellers and brokers

Compliance Corner: Establishing a Compliant Trust Account

SC REC Newsletter January 2019

If taking possession of funds belonging to others in a real estate transaction, a broker in charge or property manager in charge is required to establish a properly designated Trust Account to safeguard those held funds. "Trust Account" is defined in SC Code of Laws Section 40-57-30(31). SC Code of Laws 40-57-136 goes further into the compliance requirements for creating, designating and maintaining trust funds.

A Real Estate trust account for purposes of South Carolina compliance must:

- Be a demand deposit account.

- Be in an insured financial institution authorized to do business in South Carolina.
- Be established in the name of the company or brokerage holding the funds.
- Be designated to include the word "Trust" or "Escrow" in the account title.
- Have "Trust" or "Escrow" in the account designation of checks and statements issued in connection with the account.

The Commission often receives calls from individuals who are at a bank branch and are being told that bank staff cannot or does not know how to set up a Real Estate Trust Account. The bullet points above should assist with explaining how you need to set up your account for compliance with the licensing law. The words "Trust" or "Escrow" in the account title are critical in the event of financial insolvency or default of the company as they will alert potential creditors or claimants that the funds in this account do not belong to the company.

The broker in charge or property manager in charge must maintain control and responsibility for the account if their company is taking possession of the funds. The broker in charge or property manager in charge also must be responsible for the maintenance of records relating to the accounts, all related transactions, and the monthly reconciliation of the accounts.

If the company has multiple offices, it may utilize one centralized trust account, however, there must be a responsible broker in charge or property manager in charge for this account and for account record keeping and reconciliation.

Trust funds should not be commingled with other brokerage or licensee funds or be treated as an operating account. The Commission is beginning work on an updated Trust Account Guidelines document that will be educational for licensees who are currently or who are interested in becoming a broker in charge or property manager in charge. Please note: a trust account under current law is not required to be maintained by the "In Charge" licensee if the brokerage will not be taking possession of funds and instead utilizing a third-party escrow agent such as an attorney. The use of a third-party trust agent should be agreed upon by the parties in the contracts utilized by the brokerage or management company.

South Carolina Real Estate Commission

Electronic Rent/Deposit Payments Task Force Recommendation (10/19/2016)

Task Force Members:

Johnathan Stackhouse - Commissioner
Rod Atkinson – Commission Administrator
Georgia Lewis – Commission Advice Counsel
Christa Bell – Assistant Deputy Director, LLR - Office of Investigations and Enforcement
Austin Smallwood – Staff Attorney, SCR
Eric Wetherington – Broker in Charge – Carolina One Property Management

The South Carolina Real Estate Commission is tasked with regulation of the licensed practice of Real Estate agency in the State of South Carolina and the protection of the public through its authority granted in S.C. Code of Laws Title 40, Chapter 57. The following applicable provisions address licensee’s responsibilities to receive, maintain, account for and protect trust funds.

S.C. Code of Laws Section 40-57-30 (2017)

(4) ‘Broker-in-charge’ means a broker designated to have responsibility over the actions of all associated licensees and also has the responsibility and control over and liability for a real estate trust account.

(21) ‘Property manager-in-charge’ means a property manager who is designated as having the responsibility over the actions of associated licensees and also the responsibility and control over and liability for real estate trust accounts.

(31) ‘Trust account’ means an escrow account or properly designated demand deposit bank account that is:

(a) properly designated and title to which includes the words ‘trust’ or ‘escrow’; and

(b) established and maintained by a broker-in-charge or a property manager-in-charge to safeguard funds belonging to parties to a real estate transaction.

(32) ‘Trust funds’ means funds received on behalf of another person by a licensee in the course of performing a real estate activity.

S.C. Code of Laws Section 40-57-136 (B) (2017)

(B)(1)A broker-in-charge or property manager-in-charge shall ensure that accurate and complete records, as required by this chapter, are maintained for real estate trust accounts.

(4) Trust funds received by a licensee in connection with a real estate transaction in which the licensee is engaged for the broker-in-charge or property manager-in-charge must be delivered to the broker-in-charge or property manager-in-charge no later than the following business day.

S.C. Code of Laws Section 40-57-136(C)(1) (2017)

(C)(1)(a) Except as provided in subitem (b), trust funds received by a broker-in-charge or property manager-in-charge in a real estate rental or lease transaction must be deposited as follows in a real estate trust account as follows:

(i) cash or certified funds must be deposited within forty-eight hours of receipt, excluding Saturday, Sunday, and bank holidays; and

(ii) checks must be deposited within forty-eight hours after a lease or rental agreement is signed by the parties to the transaction, excluding Saturday, Sunday, and bank holidays.

(b) Rent received by a licensee who is directly employed by the owner of rental property may be deposited in an operating or other similar account, but otherwise must be properly accounted for as provided in this section. However, an advance rental deposit is a trust fund and must be treated as such.

With the understanding that the “in charge” licensee still retains and cannot delegate the responsibilities to keep records, reconcile and maintain trust accounts, the Task Force is recommending that when a licensee chooses to utilize the service of a 3rd party electronic payment processor for the receipt of trust funds in a real estate transaction, which includes rental, leasing and sales transactions, that there be written disclosures in the contract which creates the obligation for the party submitting the funds.

The disclosure should include:

1. The name of the company who will be processing and in custody of the trust fund payments.
2. The full contact information of the company who will be processing and in custody of the trust fund payments, including address phone number and e-mail address.
3. The processing time for the trust fund payment and remittance to the brokerage firm or property management company.
4. A signature or initial acknowledgement by the payor that the payor consents to submit payment of trust funds to the brokerage firm or property management company through the 3rd party company and understands that the funds will not be placed into the brokerage firm or property management company’s trust account until payments are remitted by the 3rd party company.
5. Any fees affiliated with the payments in the real estate transaction which are the responsibility of the payor.

Sample 4-way Crosscheck Worksheet

Identify contracts with outstanding earnest money deposits, leases with security or other deposits, other outstanding trust items, and BIC funds in trust account. List the open contracts and leases and total.

Total Earnest money deposits from open contracts _____

Total Security or other deposits from leases _____

BIC personal funds _____

1. Total open trust funds from above _____

2. What is checkbook balance? _____

3. What is general ledger balance? _____

4. Total subaccount ledger balances _____

Are all four totals the same? Yes or No

If no, explain.