SB 507

Department of Legislative Services

Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 507 (Senator Kelley, *et al.*)
Finance Economic Matters

Financial Institutions - Interest Payable on Escrow Accounts and Specific Purpose Savings Accounts

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This bill alters the method used to calculate the amount of interest paid by (1) a lending institution on an escrow account created in connection with a loan, including a closed-end credit transaction, secured by a first mortgage or first deed of trust; and (2) a banking institution on each interest-bearing account that is instituted for a specific purpose for a period of one year or less.

The bill takes effect June 1, 2012, and applies to escrow accounts and savings accounts established on or after June 1, 2012.

Fiscal Summary

State Effect: The bill does not directly affect governmental operations or finances.

Local Effect: The bill does not directly affect local governmental operations or finances.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: The bill requires the amount of interest to be an annual rate not less than the six-month average dealer bid rate on nationally traded certificates of deposits, as published by the Federal Reserve in "Selected Interest Rates (Daily) – H.15," as of the first business day of the calendar year. For lending institutions, the amount of interest must be adjusted, if applicable, as of the first day of each calendar year to reflect the rate to be paid during that year.

Current Law:

Escrow Accounts: If a specified lending institution creates, or is the assignee of, an escrow account in connection with a loan, including a closed-end credit transaction, secured by a first mortgage or first deed of trust on any interest in residential real property, the lending institution must pay interest to the borrower on the funds in the escrow at the greater of 3% per annum simple interest or the rate of interest regularly paid by the lending institution on regular passbook savings accounts. The lending institution must provide the borrower with an escrow account statement each year and pay annual interest, computed on the account's average monthly balance, by crediting the escrow account with the amount due.

Maryland's requirements to pay a specified amount of interest and provide a statement for an escrow account created for a loan secured by a first mortgage or first deed of trust on any interest in residential real property do not apply if the loan is purchased by an out-of-state lender through the Federal National Mortgage Association, the Government National Mortgage Association, or the Federal Home Loan Mortgage Corporation and the out-of-state lender, as a condition of purchase, elects to service the loan. However, they do apply if the out-of-state lender sells the loan to a Maryland lender or places the loan with a Maryland lender for servicing.

If the purpose of the escrow account is to pay taxes, insurance premiums, and ground rents, the account funds may not be used to reduce principal or pay interest or other loan charges, except in a foreclosure, release, or situation in which the escrow account balance exceeds the amount provided for in the note, loan agreement, or security instrument. If the balance does periodically exceed the amount provided for in the note, loan agreement, or security instrument, the lending institution must give the borrower the option of (1) receiving a refund of the excess amount; (2) applying the excess amount to the payment of principal and interest; or (3) leaving the excess amount in the escrow account. Any refund of an excess amount must be made within 60 days after the receipt by the lender of the borrower's request for a refund. However, if the borrower has not yet notified the lender of the option chosen, the lender must refund any excess amount within 60 days after the date the lender mailed notice of the excess amount to the borrower.

Specific Purpose Accounts: A banking institution must pay at least 3% annual interest on each interest-bearing account that is instituted for a specific purpose, including "Christmas" or "vacation" accounts, for a period of one year or less.

Background: A financial institution may require borrowers of loans secured by mortgaged property to place funds into an escrow account. The funds maintained in the escrow account are then used to pay annual taxes and insurance on the mortgaged property. While the financial institution generally determines whether the borrower must maintain an escrow account, financial institutions are required to establish escrow accounts for some federal programs, including any Federal Housing Administration-insured loans. The Real Estate Settlement Procedures Act (RESPA) allows a financial institution to collect escrow payments one-sixth greater than the estimated year-end tax and insurance amounts. However, if state law or mortgage documents allow for a lesser amount, the financial institution may only collect the lesser amount. RESPA further requires the financial institution to perform an annual escrow account analysis and provide the borrower with initial and annual escrow account statements. If the annual escrow account analysis reveals a shortage or a deficiency, RESPA provides a loan servicer with several options in order to collect repayment from a borrower.

Exhibit 1 shows the six-month average dealer bid rate on nationally traded certificates of deposit (CDs), as published by the Federal Reserve in "Selected Interest Rates (Daily) – H.15," as of the first business day of the calendar year.

Exhibit 1
2003-2012 Six-month Average Dealer Bid Rate on Certificates of Deposit

Year	Rate
2012	0.64%
2011	0.39%
2010	0.29%
2009	1.70%
2008	4.58%
2007	5.32%
2006	4.68%
2005	2.73%
2004	1.15%
2003	1.31%

Source: Federal Reserve Board

Small Business Effect: The bill has a potentially meaningful effect on in-state financial institutions, some of which are small businesses. Under current law, a financial institution must pay interest to a borrower on the funds in the escrow account at the greater of 3% per annum simple interest or the rate of interest regularly paid by the lending institution on regular passbook savings accounts. Additionally, financial institutions must pay at least 3% annual interest on each interest-bearing account that is instituted for a specific purpose for a period of one year or less.

Under the bill, if the six-month average dealer bid rate on nationally traded CDs remains at its current level, financial institutions could realize meaningful savings. The magnitude of savings would depend on the number of accounts, the amount of funds in each account, and the length of time the funds are held in the account.

It should be noted, however, that despite the potential savings for financial institutions due to recent low rates on CDs, in the future, lending institutions may be required to return an amount of interest greater than the current requirement to the extent that the six-month average dealer bid rate on CDs exceeds 3%.

Additional Information

Prior Introductions: None.

Cross File: HB 533 (Delegate Feldman, *et al.*) - Economic Matters.

Information Source(s): Judiciary (Administrative Office of the Courts); Department of Labor, Licensing, and Regulation; Department of Legislative Services

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