Escrow

An escrow is any arrangement where two parties agree to have a third party receive, hold and disburse funds and execute mutually agreed-upon instructions. In the context of buying your home, you'll encounter two escrows. One begins when your offer is accepted by the seller and ends when you close. The other begins when you close and ends when you pay off your mortgage.

Facilitating Closing through Escrow

The first escrow is all about the nuts and bolts of getting your transaction closed. Your escrow agent is a neutral third party, taking in instructions from everybody involved in your transaction (you, seller, lenders, Realtors, contractors, insurance agents and more), makes sure everybody is on the same page and then facilitates closing.

It's important stuff: They are in charge of holding and disbursing funds and documents. They handle payment of all liens and other encumbrances. They do all necessary accounting and handle administrative details. And if at any point they receive conflicting instructions, they bring it to everybody's attention and hold off on closing until they receive clarification.

In Oregon and Washington (and most of the West), title companies act as escrow agents. When you and the seller reach mutually acceptable terms for the purchase of a home, the real estate agent representing the seller will open escrow with a title company. You will generally write your earnest money check to the title company. And you will go to their office (or otherwise make arrangements with them) to sign all of your closing papers. It is at closing that your second escrow is opened.

Property Tax and Insurance Escrow

Most (but not all) mortgages have an escrow account for taxes and homeowners insurance. If your loan has an escrow account, you pay one twelfth of your taxes and insurance together with your loan payment each month. Each month, your lender deposits these funds into an escrow account. When taxes and insurance come due, your lender pays them, from this account. If you are not sure you have an escrow account, you can look for deposits to one on page 2 of your HUD-1 settlement statement from closing, mention of one on your monthly loan statement, or just call us.

Annual escrow review

Every year, usually in January, your loan servicer will analyze your escrow account. You'll receive a statement showing what you paid in and what your lender paid out through the year. At its low point (typically right after your taxes are paid), your escrow should still have a balance equal to a month or two of taxes, a cushion to allow for increases.

Like everything else in life (sigh), you can pretty much count on taxes and insurance increasing. As a result, expect that your escrow will have a bit of shortage each year. Usually, you will be given two

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options to remedy the shortage

1. Your lender will adjust your monthly payment to include an extra amount each month to pay back the shortage in installments.
2. Your can write a check for the shortage.

The first option is a tiny way to get one over on The Man. Your loan servicer paid your taxes and insurance, effectively spotting you the shortage. If the payment is affordable, why not take what is basically an interest-free loan? Just remember that your monthly payment will increase by enough to pay back the shortage and save for the right amount next year.

If you elect to pay the shortage in a lump sum, your payment will still adjust, but only by the actual difference in taxes and insurance.

Important note regarding automatic payments: If you've set up an automatic payment through your loan servicer, your payment will automatically change. But if you have an automatic payment set up through your bank's bill payment service, watch closely for your annual escrow account statement and make sure you adjust your payment. Late fees, damaged credit and frowny faces can result if you don't.

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