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BRE Course and Instructor Evaluation

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PREFACE:

This is the textbook for our course, *Trust Funds, 2\textsuperscript{nd} Edition*. It is one of the five, three-hour courses required by the BRE for licensees renewing for the first time. Licensees renewing after the first time must take these same courses OR take an eight-hour survey course that covers these same topics (we do not offer a survey course). The five three hour courses are:

1. **Ethics:** Describes the real estate license law enforced by the BRE and the *Code of Ethics and Professional Conduct* as practiced by members of the National Association of REALTORS®.

2. **Agency:** Explains the common law of agency as applied to California real estate brokerage.

3. **Trust Funds:** Details the fiduciary responsibilities of brokers when acting as escrows for their clients' real estate transactions.

4. **Fair Housing:** Describes the federal and California fair housing and lending laws.

5. **Risk Management:** Provides licensees with the knowledge needed to avoid costly disputes with their clients arising from professional errors and omissions in the performance of their duties.

To save space and make the text more readable, we use the following abbreviations and terms:

- **BPC** — The Business and Professional Code of California.
- **BRE** — Bureau of Real Estate (starting July 2013, the Department will be called the Bureau of Real Estate).
- **CAR®** — California Association of REALTOR®s.
- **CC** — The Civil Code of California

You can find the complete California codes at [www.leginfo.ca.gov/calaw.html](http://www.leginfo.ca.gov/calaw.html). Unless otherwise stated, all cases are California cases. In citing cases, we specify only the names of the litigants and the year of the decision.

The forms cited in this course are from the California Association of REALTORS®.

In addition to the above terms and abbreviations, we also follow a few typographic conventions.

We use margin notes to provide definitions and short footnotes. We use the symbol \( \textcircled{C} \) to direct your attention to an adjacent margin note.

Side bars like this one are used for long notes. Content in the margin notes, side bars, and in the appendices is not tested in the final exam.
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Editor’s Note
The majority of this course’s content is from the chapter “Trust” in the BRE’s Reference Book.

The course makes many references to the California Code and the BRE Regulations which you can find online at these sites:

- California Codes.
- BRE’s Regulations.

We provide margin notes to define legal terms with which you may be unfamiliar. We distinguish our comments and notes from BRE’s using sidebars such as this one.

Course Introduction
Real estate brokers and salespersons receive trust funds in the normal course of doing business. They receive these funds on behalf of others, thereby creating a fiduciary responsibility to the funds’ owners. Brokers and salespersons must handle, control, and account for these trust funds according to established legal standards. While compliance with these standards may not necessarily have a direct bearing on the financial success of a real estate business, non-compliance can result in unfavorable business consequences. Improper handling of trust funds is cause for revocation or suspension of a real estate license, not to mention the possibility of being held financially liable for damages incurred by clients.

This course discusses the legal requirements for receiving and handling trust funds in real estate transactions as set forth in the Real Estate Law and the Regulations of the Real Estate Commissioner. It describes the requisites for maintaining a trust fund bank account and the precautions a licensee should take to ensure the integrity of the account. It explains and illustrates the trust fund record keeping requirements under the BPC and the BRE Regulations.

The discussions and examples in this course involve real property sales and property management trust account transactions. Other types of real estate activities involving trust funds, although subject to the same laws and regulations, may also have to comply with additional legal and regulatory requirements. While these other types of transactions may require records significantly different from those illustrated, the record keeping fundamentals still apply.
2.1 TRUST FUNDS AND NON-TRUST FUNDS

Since trust funds must be handled in a special manner, a licensee must be able to distinguish trust funds from non-trust funds. Trust funds are money or other things of value that are received by a broker or salesperson on behalf of a principal or any other person and which are held for the benefit of others in the performance of any acts for which a real estate license is required. Trust funds may be cash or non-cash items. Some examples are; cash; a check used as a purchase deposit (whether made payable to the broker or to an escrow or title company); a personal note made payable to the seller; or even an automobile’s “pink slip” given as a deposit.

The discussions in this course pertain to real estate trust funds received by licensees, and not to non-trust funds such as real estate commissions, general operating funds, and rents and deposits from broker-owned real estate. These other types of funds, as long as not commingled with trust funds, are not subject to the Real Estate Law and BRE Regulations. It should be noted, however, that under certain circumstances the BRE does have the jurisdiction to look into transactions involving non-trust funds.

2.2 WHY A TRUST ACCOUNT?

A trust account is set up as a means to separate trust funds from non-trust funds. Although it can certainly be argued that keeping trust funds in a trust account will not prevent a dishonest broker from misusing the funds, separating client's funds from the broker's own funds provides a better physical and accounting control over the trust funds.

An important reason for designating a trust fund depository as a trust account is the protection afforded principals’ funds in situations where legal action is taken against the broker or if the broker becomes incapacitated or dies. Trust funds held in a true trust account cannot be “frozen” pending litigation against the broker or during probate.

Trust funds also have better insurance protection if deposited into a trust account. The general counsel of the FDIC, in an opinion in 1965, held that funds of various owners which are placed in a custodial deposit (trust account) in an insured bank will be recognized for insurance purposes to the same extent as if the owners' names and interests in the account are individually disclosed on the records of the bank, provided the trust account is specifically designated as custodial and the name and interest of each owner of funds in the account are disclosed on the depositor's records. Each client with funds deposited in a trust account maintained with a federally insured bank is insured by the FDIC up to $250,000, as opposed to just $250,000 for the entire account, as long as the regulatory requirements are met.
2.3 Trust Fund Handling Requirements

**Neutral Escrow Depository:** Any account established by an agent to manage the funds of his principal.

A typical trust fund transaction begins with the broker or salesperson receiving trust funds from a principal in connection with the purchase or lease of real property. According to BPC §10145, trust funds received must be placed into the hands of the owner(s) of the funds, into a neutral escrow depository, or into a trust account maintained pursuant to BRE Reg 2832 not later than three business days following receipt of the funds by the broker or by the broker’s salesperson.

An exception to this rule is when a check is received from an offeror in connection with an offer to purchase or lease real property. As provided under BRE Reg. 2832, a deposit check may be held uncashed by the broker until acceptance of the offer if the following conditions are met:

1. the check by its terms is not negotiable by the broker, or the offeror has given written instructions that the check shall not be deposited or cashed until acceptance of the offer; and
2. the offeree is informed, before or at the time the offer is presented for acceptance, that the check is being held.

If the offer is later accepted, the broker may continue to hold the check undeposited only if the broker receives written authorization from the offeree to do so. Otherwise, the check must be placed, not later than three business days after acceptance, into a neutral escrow depository or into the trust fund bank account, or into the hands of the offeree if both the offeror and offeree expressly so provide in writing.

According to BPC §10145, a real estate salesperson who accepts trust funds on behalf of the broker under whom he or she is licensed must immediately deliver the funds to the broker or, if directed to do so by the broker, place the funds into the hands of the broker’s principal or into a neutral escrow depository or deposit the funds into the broker’s trust fund bank account.

2.4 Identifying Owners of Trust Funds

**Offeror:** e.g., buyer  
**Offeree:** e.g., seller

A broker must be able to identify who owns the trust funds and who is entitled to receive them, since these funds can be disposed of only upon the authorization of that person. The person entitled to the funds may or may not be the person who originally gave the funds to the broker or the salesperson. In some instances the party entitled to the funds will change upon the occurrence of certain events in the transaction. For example, in a transaction involving an offer to buy or lease real property or a business opportunity, the party entitled to the funds received from the offeror (prospective buyer or lessee) will depend upon whether or not the offer has been accepted by the offeree (seller or landlord).

Prior to the acceptance of the offer, the funds received from the offeror belong to that person and must be handled according to his/her
instructions. If the funds are deposited in a trust fund bank account, they must be maintained there for the benefit of the offeror until acceptance of the offer. Or, as discussed in the previous section, if the offeror wishes, his/her check may be held uncashed by the broker as long as he/she gives written instructions to the broker to do so and the offeree is informed before or at the time the offer is presented for acceptance that the check is being so held.

*Typically the offeror is the buyer and the offeree is the seller*

After acceptance of the offer, the funds shall be handled according to instructions from the offeror and the offeree as follows:

- An offeror’s check held uncashed by the broker before acceptance of the offer may continue to be held uncashed after acceptance of the offer, only upon written authorization from the offeree (BRE Reg. 2832(d)).
- The offeror’s check may be given to the offeree only if the offeror and offeree expressly so provide in writing (BRE Reg. 2832(d)).
- All or part of an offeror’s purchase money deposit in a real estate sales transaction shall not be refunded by an agent or subagent of the seller without the express written permission of the offeree to make the refund.

### 3 Trust Fund Bank Accounts

#### 3.1 General Requirements

A neutral escrow depository is an escrow company. In California, escrow companies must be licensed.

Recognized depository would be any form of bank having its deposits insured by the FDIC; e.g. credit union, savings bank, retail bank.

Trust funds, such as a purchase money deposit check, received by a licensee that are not forwarded directly to the broker’s principal or to a neutral escrow depository or for which the broker does not have authorization to hold uncashed must be deposited to the broker’s trust fund bank account (BPC §10145).

BPC §10145 and BRE Reg. 2832 require that a trust account meet the following criteria:

1. designated as a trust account in the name of the broker as trustee;
2. maintained with a bank or recognized depository located in California; and
3. not an interest-bearing account for which prior written notice can, by law or regulation, be required by the financial institution as a condition to withdrawal (see 3.3 below for a discussion of “Interest-Bearing Accounts”)

A broker may have an out-of-state trust account if the account is insured by the Federal Deposit Insurance Corporation (FDIC) and is used to service first loans for the types of note owners/investors specified in BPC §10145(a)(2).
In other words, the broker may only use a bank outside of California for his trust fund if he services (i.e., collects payments) first mortgages on behalf of banks, corporations, trusts, and other types of substantial investors detailed in BPC § 10145(a)(2).

### 3.2 TRUST ACCOUNT WITHDRAWALS

According to BRE Reg. 2834, withdrawals from the trust account may be made only upon the signature of one or more of the following:

1. the broker in whose name the account is maintained;
2. the designated broker-officer if the account is in the name of a corporate broker;
3. if specifically authorized in writing by the broker, a salesperson licensed to the broker; or
4. if specifically authorized in writing by the broker who is a signatory of the trust account, an unlicensed employee of the broker covered by a fidelity bond at least equal to the maximum amount of trust funds to which the employee has access at any time.

No arrangement under which a person named in items 3 or 4 is authorized to make withdrawals from a broker's trust fund relieves an individual broker or the broker-officer of a corporate broker licensee from responsibility or liability as provided by law in handling trust funds in the broker's custody.

### 3.3 INTEREST-BEARING ACCOUNTS

A trust fund bank account normally may not be interest-bearing. A broker may, however, at the request of the owner of trust funds, or of the principals to a transaction or series of transactions from whom the broker has received trust funds, deposit the funds into an interest-bearing account in a bank or savings and loan association if all of the following requirements of BPC §10145(d) are met:

1. The account is in the name of the broker as trustee for a specified beneficiary or specified principal of a transaction or series of transactions.
2. All of the funds in the account are covered by insurance provided by an agency of the federal government.
3. The funds in the account are kept separate, distinct, and apart from funds belonging to the broker or to any other person for whom the broker holds funds in trust.
4. The broker discloses the following information to the person from whom the trust funds are received and to any beneficiary whose identity is known to the broker at the time of establishing the account:
the nature of the account;
• how the interest will be calculated and paid under various circumstances;
• whether service charges will be paid to the depository and by whom; and
• possible notice requirements or penalties for withdrawal of funds from the account.

5. No interest earned on funds in the account shall inure directly or indirectly to the benefit of the broker or to any person licensed to the broker, even if the funds’ owners would permit such an arrangement.

6. In an executory sale, lease, or loan transaction in which the broker accepts funds in trust to be applied to the purchase, lease, or loan, the parties to the contract shall have specified in the contract or by collateral written agreement the person to whom interest earned on the funds is to be paid or credited.

The only other situation where a real estate broker is allowed to deposit trust funds into an interest-bearing account occurs when the broker is acting as an agent for a financial institution which is the beneficiary of a loan. In this case the broker may, pursuant to BRE Reg, 2830.1, deposit and maintain funds received from or for the account of an obligor (borrower) into an interest-bearing trust account in a bank or savings and loan association in order to pay interest on an impound account to the obligor in accordance with CC §2954.8, as long as the following requirements are met:

These are better known as “escrow impound accounts” – accounts which lenders create to collect “up-front” money from the borrower when he takes out a mortgage to cover future expenses such as property taxes and insurance.

1. The funds received from or for the account of the obligor are for the future payment of property taxes, assessments, or insurance relating only to a property containing a one-to-four family residence.
2. The account is in the name of the broker as trustee.
3. All of the funds in the account are covered by insurance provided by an agency of the federal government.
4. All of the funds in the account are funds held in trust by the broker for others.
5. The broker discloses to the obligor how interest will be calculated and paid.
6. No interest earned on the trust funds shall inure directly or indirectly to the benefit of the broker or to any person licensed to the broker.
3.4 COMMINGLING PROHIBITED

Funds belonging to a licensee may not be commingled with trust funds. Commingling is strictly prohibited by the Real Estate Law. It is grounds for the revocation or suspension of a real estate license pursuant to BPC §10176(e).

Commingling occurs when:

1. Personal or company funds are deposited into the trust fund bank account. *Except for what is provided in §2835 of the BRE Regulations as noted below, this is a violation of the law even if separate records are kept.*

2. Trust funds are deposited into the licensee's general or personal bank account rather than into the trust fund account. In this case the violation is not only commingling, but also handling trust funds contrary to BPC §10145. It is also grounds for suspension or revocation of a license under BPC §10177(d).

3. Commissions, fees, or other income earned by the broker and collectible from the trust account are left in the trust account for more than 25 days from the date they were earned.

A common example of commingling is depositing rents and security deposits on broker owned properties into the trust account. As these funds relate to the broker's properties, they are not trust funds and, therefore, may not be deposited into the trust fund bank account. Likewise, the broker may not make mortgage payments and other payments on broker-owned properties from the trust account even if the broker reimburses the account for such payments. Conducting personal business through the trust account is strictly prohibited and is a violation of the Real Estate Law.

A real estate broker's personal funds may be in the trust account in the following two specific instances:

1. Up to $200 to cover checking account service fees and other bank charges such as check printing charges and service fees on returned checks. Trust funds may not be used to pay for these expenses. (The preferred practice, however, is for the broker to have the bank debit his/her own personal account for any trust account fees and charges.)

2. Commissions, fees, and other income earned by a broker and collectible from trust funds may remain in the trust account for a period not to exceed 25 days. BRE Reg. 2835 recognizes that it may not always be practical to disburse the earned income immediately upon receipt. For instance, a property management company may find it too burdensome to collect its management fee every time a rent check is received and deposited to the trust account. Therefore, as long as the broker disburses the fee from the trust account within 25 days after deposit there is no commingling violation. Note, however, that income earned shall not be taken from trust funds received before depositing such funds into
the trust bank account. Also, under no circumstances may the broker pay personal obligations from the trust fund bank account even if such payments are a draw against commissions or other income. The broker must issue a trust account check to himself for the total amount of the income earned, adequately documenting such payment, and then pay personal obligations from the proceeds of that check.

3.5 **TRUST FUND LIABILITY**

Trust fund liability arises when funds are received from or for the benefit of a principal. The aggregate trust fund liability at any one time for a trust account with multiple beneficiaries is equal to the total *positive* balances due to all beneficiaries of the account at the time. Note that beneficiary accounts with negative balances are not deducted from other accounts when calculating the aggregate trust fund liability.

Funds on deposit in the trust account must always equal the broker’s aggregate trust fund liability. If the trust account balance is *less* than the total liability, a *trust fund shortage* results. Such a shortage is in violation of BRE Reg. 2832.1 which states that the written consent of every principal who is an owner of the funds in the account shall be obtained by a real estate broker prior to each disbursement if such a disbursement will reduce the balance of the funds in the account to an amount less than the existing aggregate trust fund liability of the broker to all owners of the funds. Conversely, if the trust account balance is *greater* than the total liability, there is a *trust fund overage* and the broker may be in violation of BPC §10176(e) for commingling.

**Editors Note**

The forms referenced below are available [here](#) from the BRE’s website: In the below table, the “Short Name” column is the name by which the form is referenced in this course; “Complete Name” is the actual name of the form’s title. We have modified the text of this chapter to use the short names for the various forms followed by the form number (e.g., “Bank Account Record [#4522]”).

<table>
<thead>
<tr>
<th>Form</th>
<th>Short Name/Description</th>
<th>Complete Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>#4521</td>
<td>Bank Account Record: One line for each deposit or withdrawal from the account.</td>
<td>Trust Fund Record Keeping Information</td>
</tr>
<tr>
<td>#4522</td>
<td>Separate Beneficiary Record: One record for each beneficiary. Each line records a deposit or withdrawal affecting the beneficiary’s balance.</td>
<td>Columnar Record of all Trust Funds Received and Paid Out -- Trust Fund Bank Account</td>
</tr>
<tr>
<td>#4523</td>
<td>Record of Undeposited Receipts: Funds received in trust but not deposited to the trust fund account (e.g., undeposited checks).</td>
<td>Separate Record for each Beneficiary or Transaction For Client's Funds Placed in Trust Funds Placed in Trust Fund Bank Account</td>
</tr>
<tr>
<td>#4524</td>
<td>Separate Property Record: One record for each property (similar to #4523 but based on a property instead of a beneficiary). Each line records a deposit or withdrawal affecting the property.</td>
<td>Record for All Trust Funds Received -- Not Placed in Broker's Trust Account</td>
</tr>
<tr>
<td>#4525</td>
<td></td>
<td>Separate Record for each Property Managed.</td>
</tr>
</tbody>
</table>
Examples of these forms are given in Exhibits 1-10 at the end of this chapter.

A trust fund discrepancy of any kind is a serious violation of the Real Estate Brokerage Act. Many real estate licenses have been revoked after a BRE audit disclosed a trust account shortage. To ensure that the balance of the trust account always equals the trust fund liabilities, a broker should implement the following procedures:

1. Deposit intact and in a timely manner to the trust account all funds that are not forwarded to escrow or to the funds’ owner(s) or which are not held uncashed as authorized. This practice, required under BRE Reg. 2832, lessens the risk of the funds being lost, misplaced, or otherwise not deposited to the trust account. A licensee is accountable for all trust funds received whether or not they are deposited. BRE auditors have seen numerous cases where trust funds received were properly recorded on the books but were never deposited to the trust account.

2. Maintain adequate supporting papers for any disbursement from the trust account. Record the disbursement accurately in both the Bank Account Record [#4522] and the Separate Beneficiary Record [#4523]. The broker must be able to account for all disbursements of trust funds. Any unidentified disbursement will cause a shortage.

3. Disburse funds from a beneficiary’s account only when the disbursement will not result in a negative or deficit balance (negative accountability) in the account. Many trust fund shortages are caused by disbursements to a beneficiary in excess of funds received from or for account of that beneficiary. The excess disbursements are, in effect, paid out of funds belonging to other beneficiaries. A shortage occurs because the balance of the trust fund bank account, even if it is a positive balance, is less than the broker’s liability to the other beneficiaries.

4. Ensure that a check deposited to the trust fund account has cleared before disbursing funds against that check. This applies, for example, when a broker who has deposited an earnest money check for a purchase transaction has to return the funds to the buyer because the offer is rejected by the seller. A trust fund shortage will result if the broker issues the buyer a trust account check and the buyer’s deposit check bounces or for some reason fails to clear the bank.

5. Keep accurate, current and complete records of the trust account and the separate record for each beneficiary. These records are essential to ensure that disbursements are correct.

6. On a monthly basis, reconcile the cash record with the bank statement and with the separate record for each beneficiary or transaction.
3.6 SUMMARY

In summary, to maintain the integrity of the trust fund bank account, a broker must ensure that:

1. his/her personal or general operating funds are not commingled with trust funds;
2. the balance of the trust fund account is equal to the broker’s trust fund liability to all owners of the funds; and
3. the trust fund records are in an acceptable form and are current, complete and accurate.

4 ACCOUNTING RECORDS

4.1 GENERAL REQUIREMENTS

An important aspect of the broker’s fiduciary responsibility to the client is the maintenance of adequate records to account for trust funds received and disbursed. This is true whether the funds are deposited to the trust fund bank account, sent to escrow, held uncashed as authorized under BRE Reg. 2832, or released to the owner(s) of the funds. These records:

1. provide a basis upon which the broker can prepare an accurate accounting for clients.
2. state the amount of money the broker owes the account beneficiaries at any one time. (This is especially important when there are a large number of transactions.)
3. prove whether or not there is an imbalance in the trust account. Some brokers audited by BRE have disagreed that their trust accounts had a shortage or an overage in the amount disclosed by the audit, but could not provide documentation to support their position.
4. guarantee that beneficiary funds deposited in the trust account will be insured up to the maximum FDIC insurance coverage.

There are two types of accounting records that may be used for trust funds: columnar records in the formats prescribed by BRE Reg. 2831 and 2831.1; and records other than columnar that are in accordance with generally accepted accounting practices which include details specified in subdivision (a) of the Regulations and are in a format that will readily enable tracing and reconciliation in accordance with 2831.2. Regardless of the type of records used, they must include the following information:

1. all trust fund receipts and disbursements, with pertinent details, presented in chronological sequence;
2. the balance of the trust fund account, based on recorded transactions;

3. all receipts and disbursements affecting each beneficiary’s balance, presented in chronological sequence; and

4. the balance owing to each beneficiary or for each transaction.

Either manually produced or computerized accounting records are acceptable. The type and form of records appropriate to a particular real estate operation as well as the means of processing transactions will depend on factors such as the nature of the business, the number of clients, the volume of transactions, and the types of reports needed. For example, manual recording on columnar records might be satisfactory for a broker handling a small number of transactions, while a computerized system might be more appropriate and practical for a large property management operation.

### 4.2 COLUMNAR RECORDS

A broker may decide to use the columnar records prescribed by BRE Reg. 2831 and 2831.1. The records required will depend on whether the trust funds received are deposited to the trust account or are forwarded to an escrow depository or to the owner of the funds. These records are:

1. Bank Account Record [#4522];
2. Separate Beneficiary Record [#4523]; and
3. Record of Undeposited Receipts [#4524].

The first two records are required when trust funds are received and deposited to the trust fund bank account. The third record is required when trust funds received are not deposited to the trust account, but are instead forwarded to the authorized person(s).

If the trust fund account involves clients’ funds from rental properties managed by the broker, the Separate Property Record [#4525] may be used in lieu of the Separate Beneficiary Record [#4523].

A broker who has an escrow division pursuant to Financial Code §17006(a)(4) must keep the above mentioned records for escrow funds. (BRE Reg. 2951)

### 4.3 BANK ACCOUNT RECORD [#4522]

**COLUMNAR RECORD OF ALL TRUST FUNDS RECEIVED AND PAID OUT**

<table>
<thead>
<tr>
<th>Date Received</th>
<th>From Whom Received or To Whom Paid</th>
<th>Description</th>
<th>Received Amount</th>
<th>Reference</th>
<th>Date of Deposit</th>
<th>XX</th>
<th>Paid Out Amount</th>
<th>Check Number</th>
<th>Date of Check</th>
<th>XX</th>
<th>Daily Balance of Trust Bank Account</th>
</tr>
</thead>
</table>
This record is used to journalize all trust funds deposited to and disbursed from the trust fund bank account. At a minimum, it must show the following information in columnar form: date funds were received; name of payee or payor; amount received; date of deposit; amount paid out; check number and date; and the daily balance of the trust account.

All transactions affecting the trust account are entered in chronological order on this record regardless of payee, payor, or beneficiary. If there is more than one trust fund bank account, a different columnar record must be maintained for each account, pursuant to BRE Reg. 2831.

### 4.4 SEPARATE BENEFICIARY RECORD [#4523]

<table>
<thead>
<tr>
<th>Description</th>
<th>Date of Check</th>
<th>Check Number</th>
<th>Amount</th>
<th>Date of Deposit</th>
<th>Amount</th>
<th>Account Balance</th>
</tr>
</thead>
</table>

This record is maintained to account for funds received from or for the account of each beneficiary, or for each transaction, and deposited to the trust account. With this record, the broker can ascertain the funds owed to each beneficiary or for each transaction. The record must show the following in chronological order: date of deposit; amount of deposit; name of payee or payor; check number; date and amount; and balance of the individual account after posting transactions on any date.

A separate record must be maintained for each beneficiary or transaction from whom the broker received funds that were deposited to the trust fund bank account. If the broker has more than one trust account, each account must have its own set of beneficiary records so that they can be reconciled with the individual trust fund bank account record required by BRE Reg. 2831.2.

### 4.5 RECORD OF UNDEPOSITED RECEIPTS [#4524]

This record is used to keep track of funds received and not deposited to a trust fund bank account. In this situation, the broker is handling the funds and must keep records of same. Examples are:
1. earnest money deposits forwarded to escrow;
2. rents forwarded to landlords; and
3. borrowers’ payments forwarded to lenders.

This record must show the date funds were received, the form of payment (check, note, etc.), amount received, description of property, identity of the person to whom funds were forwarded, and date of disposition. Trust fund receipts are recorded in chronological sequence, while their disposition is recorded in the same line where the corresponding receipt is recorded.

Transaction folders usually maintained by a broker for each real estate sales transaction showing the receipt and disposition of undeposited checks are not acceptable alternatives to the Record of Trust Funds Received but Not Deposited to the Trust Fund Bank Account.

An exception to this record keeping requirement is provided in BRE Reg. 2831(e), which states that a broker is not required to keep records of checks written by a principal, given to the broker, and made payable to service providers, including but not limited to escrow, credit and appraisal services, when the total amount of such checks for any transaction does not exceed $1,000. However, a broker shall retain for three years copies of receipts issued or obtained in connection with the receipt and distribution of such checks and, upon request of the Department or the maker of the checks, a broker must account for the receipt and distribution of the checks.

### 4.6 Separate Property Record [#4525]

This record is similar to, and serves the same purpose as, the Separate Beneficiary Record [#4523]. It does not have to be maintained if a separate record is already used for a property owner’s account. The Separate Property Record [#4525] is useful when the broker wants to show some detailed information about a specific property being managed.

### 5 Other Accounting Systems

A broker may use trust fund records not in the columnar form as prescribed by BRE Reg. 2831 and 2831.1. Such records must be in accordance with generally accepted accounting principles and must include detail specified in subdivision (a) of these Regulations and be in a format that will readily enable tracing and reconciliation in accordance with 2831.2. Whether prepared manually or by computer, they must include at least the following:
1. A journal to record in chronological sequence the details of all trust fund transactions.

2. A cash ledger to show the bank balance as affected by the transactions recorded in the journal. The ledger is posted in the form of debits and credits. (In some cases the cash ledger may be combined with the journal.)

3. A beneficiary ledger for each of the beneficiary accounts to show in chronological sequence the transactions affecting each beneficiary’s account, as well as the balance of the account.

To comply with generally accepted accounting principles, there must be one set of journal, cash ledger, and beneficiary ledger for each trust fund bank account.

### 5.1 Journal

A journal is a daily chronological record of trust fund receipts and disbursements. A single journal may be used to record both the receipts and the disbursements, or a separate journal may be used for each. To meet minimum record keeping requirements, a journal must:

1. Record all trust fund transactions in chronological sequence.

2. Contain sufficient information to identify the transaction such as the date, amount received or disbursed, name of or reference to payee or payor, check number or reference to another source document of the transaction, and identification of the beneficiary account affected by the transaction.

3. Correlate with the ledgers. For example, it should show the same figures that are posted, individually or in total, in the cash ledger and in the beneficiary ledgers. The details in the journal must be the basis for posting transactions on the ledgers and arriving at the account balances.

4. Show the total receipts and total disbursements regularly, at least once a month.

### 5.2 Cash Ledger

The cash ledger shows, usually in summary form, the periodic increases and decreases (debits and credits) in the trust fund bank account and the resulting account balance. It can be incorporated into the journal or it can be a separate record, for example a general ledger account. If a separate record is used, the postings must be based on the transactions recorded in the journal. The amounts posted on the ledger must be those shown in the journal.
5.3 Beneficiary Ledger

A separate beneficiary ledger must be maintained for each beneficiary or transaction or series of transactions. This ledger shows in chronological sequence the details of all receipts and disbursements related to the beneficiary’s account, and the resulting account balance. It reflects the broker’s liability to a particular beneficiary. Entries in all these ledgers must be based on entries recorded in the journal.

6 Recording Process

Keeping complete and accurate trust fund records is easier when specific procedures are regularly followed. The following procedures may be useful in developing a record keeping routine:

1. Record transactions daily in the trust fund bank account and in the separate beneficiary records.

2. Use consistently the same specific source documents as a basis for recording trust fund receipts and disbursements. (For example, receipts pertaining to real estate resales will be recorded based on the Real Estate Contract and Receipt for Deposit form, and disbursements will always be recorded based on the checks issued from the trust account or debit notices from the bank.)

3. Calculate the account balances on all applicable records at the time entries are made.

4. Reconcile the records monthly to ascertain that transactions are properly recorded on both the bank account record and the applicable subsidiary records.

5. Reconcile the trust records to the trust account bank statement on a monthly basis to ascertain that amounts per the bank are in agreement with amounts per the trust fund records.

6. If more than one trust fund bank account is maintained, keep a different set of properly labeled columnar records (cash record and beneficiary record) for each account.
7 RECONCILIATION

7.1 PURPOSE

Please keep in mind that the Separate Property Record [#4525] is a suitable replacement for the Separate Beneficiary Record [#4523] when the accounting object is a property and not a person.

The Bank Account Record [#4522], the Separate Beneficiary Record [#4523], and the bank statement are all interrelated. Any entry made on the Bank Account Record [#4522] must have a corresponding entry on a Separate Beneficiary Record [#4523]. By the same token, any entry or transaction shown on the bank statement must be reflected on the Bank Account Record [#4522]. This applies to columnar as well as to other types of records.

The accuracy of the records is verified by reconciling them at least once a month. Reconciliation is the process of comparing two or more sets of records to determine whether their balances agree. It will disclose whether the records are completed accurately.

For trust fund record keeping purposes, two reconciliations must be made at the end of each month:

1. reconciliation of the Bank Account Record [#4522] with the bank statement; and,

2. reconciliation of the Bank Account Record [#4522] with the Separate Beneficiary/Property Records [#4523, #4525].

7.2 WITH BANK STATEMENT

The reconciliation of the Bank Account Record [#4522] with the bank statement will disclose any recording errors by the broker or by the bank. If the balance on the Bank Account Record [#4522] agrees with the bank statement balance as adjusted for outstanding checks, deposits in transit, and other transactions not yet included in the bank statement, there is more assurance that the balance on the Bank Account Record [#4522] is correct.

7.3 BANK ACCOUNT RECORD [#4522] WITH EACH SEPARATE BENEFICIARY RECORD [#4523]

This reconciliation, which is required by BRE Reg. 2831.2, will substantiate that all transactions entered on the Bank Account Record [#4522] were posted on the Separate Beneficiary Records [#4523]. The balance on the Bank Account Record [#4522] should equal the total of all beneficiary record balances. Any difference should be located and the records corrected to reflect the correct bank and liabilities balances. BRE Reg. 2831.2 requires that this reconciliation process be performed monthly except in those months when there is no activity in the trust fund bank account, and that a record of each reconciliation be maintained. This record should identify the
bank account name and number, the date of the reconciliation, the account number or name of the principals or beneficiaries or transactions, and the trust fund liabilities of the broker to each of the principals, beneficiaries, or transactions.

### 7.4 Overages

When a broker performs a reconciliation pursuant to BRE Reg. 2831.2, the broker may find an unexplained overage. An unexplained overage is defined as funds in a real estate broker’s trust account which exceed the aggregate trust fund liability of such account where the broker is unable to determine the ownership of such excess funds.

Unexplained trust account overages are trust funds and unless the broker can establish the ownership of such funds the funds must be maintained in the broker’s trust fund account or in a separate trust fund account established to hold such funds.

Unexplained trust account overages may not be used to offset or cover shortages that may exist otherwise in the broker’s trust account.

A broker must keep a separate record of unexplained trust account overages including a separate subsidiary ledger to record the potential trust fund liability. Such records must include the date of recording and the date on which such funds became an unexplained trust account overage. A broker holding unexplained trust account overages must perform a monthly reconciliation of such funds in accordance with BRE Reg. 2831.2.

### 7.5 Suggestions for Reconciliation

The following is a general discussion on how to perform the trust account reconciliations.

1. Before performing the reconciliations, record all transactions up to the cut-off date in both the Bank Account Record [#4522] and the Separate Beneficiary Records [#4523].

2. Use balances as of the same cut-off date for the two records and the bank statement.

3. For the bank account reconciliation, calculate the adjusted bank balance from the bank statement and from the Bank Account Record [#4522]. (Brokers commonly err by calculating the adjusted bank balance based solely on the bank statement, ignoring the Bank Account Record [#4522]. While they may know the correct account balances, they may not realize their records are incomplete or erroneous.)

4. Keep a record of the two reconciliations performed at the end of each month along with the supporting schedules.

5. Locate any difference between the three sets of accounting records. A difference can be caused by:
not recording a transaction,
- recording an incorrect figure,
- erroneous calculations of entries used to arrive at account balances,
- missing beneficiary records, or
- bank errors.

# 8 DOCUMENT REQUIREMENTS

## 8.1 ACTIVITIES AND RELATED DOCUMENTS

In addition to accounting records, the BRE requires that the broker maintain all documents prepared or obtained in connection with any real estate transaction handled. Here is a list of typical activities and the corresponding documentation.

<table>
<thead>
<tr>
<th>Activity</th>
<th>Documentation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Receiving Trust Funds in the form of:</td>
<td>• Real estate purchase contract and receipt for deposit, signed by the buyer</td>
</tr>
<tr>
<td>Purchase deposits from buyers</td>
<td>• Collection receipts</td>
</tr>
<tr>
<td>Rents and security deposits from tenants</td>
<td>• Collection receipts</td>
</tr>
<tr>
<td>Other receipts</td>
<td></td>
</tr>
<tr>
<td>2. Depositing trust funds</td>
<td>• Bank deposit slips</td>
</tr>
<tr>
<td>3. Forwarding buyers’ checks to escrow</td>
<td>• Receipt from title/escrow company and copy of check</td>
</tr>
<tr>
<td>4. Returning buyers’ checks</td>
<td>• Copy of each buyer’s check signed and dated by buyer, signifying buyer’s receipt of check</td>
</tr>
<tr>
<td>5. Disbursing trust funds</td>
<td>• Checks issued</td>
</tr>
<tr>
<td></td>
<td>• Supporting papers for the checks, such as invoices, escrow statements, billings, receipts, etc.</td>
</tr>
<tr>
<td>6. Receiving offers and counteroffers from buyers and sellers</td>
<td>• Real estate purchase contract and receipt for deposit, signed by respective parties</td>
</tr>
<tr>
<td></td>
<td>• Agency disclosure statement</td>
</tr>
<tr>
<td></td>
<td>• Transfer disclosure statement</td>
</tr>
<tr>
<td>7. Collecting management fees from the trust fund bank account</td>
<td>• Property management agreements between broker and property owners. <strong>Note:</strong> If only one trust fund check is issued for management fees charged to various property owners, there should be a schedule or listing on file showing each property and amount charged, and the total amount, which should agree with the check</td>
</tr>
</tbody>
</table>
8. Reconciling bank account record with Separate Beneficiary Records [4524]

- Cancelled checks
- Record of reconciliation

9. **ADDITIONAL REQUIREMENTS**

The following is an additional requirement of the Real Estate Law and the BRE Regulations relating to the preparation and management of real estate transaction documents.

9.1 **SIGNERS TO BE GIVEN COPY**

Under BPC §10142, any time a licensee prepares or has prepared an agreement authorizing or employing that licensee to perform any acts for which a real estate license is required or when the licensee obtains the signature of any person to any contract pertaining to such services or transaction, the licensee must deliver a copy of the agreement to the person signing it at the time the signature is obtained. Examples of such documents are listing agreements, real estate purchase contract and receipt for deposit forms, addenda to contracts, and property management agreements.

10. **AUDITS AND EXAMINATIONS**

Because of the importance of trust fund handling, the Commissioner has an ongoing program of examining brokers’ records. As necessary, audited licensees are made aware of deficiencies in trust fund handling and record keeping. If an audit discloses actual trust fund imbalances or money handling procedures which may cause monetary loss, appropriate disciplinary proceedings are initiated.

BPC §10148 provides that a real estate broker shall retain for three years copies of all listings, deposit receipts, canceled checks, trust records, and other documents executed by or obtained by the broker in connection with any transaction for which a real estate broker license is required. The retention period shall run from the date of the closing of the transaction or from the date of the listing if the transaction is not consummated. After notice, such books, accounts and records shall be made available for examination, inspection, and copying by the Commissioner or a designated representative during regular business hours, and shall, upon the appearance of sufficient cause, be subject to audit without further notice, except that such audit shall not be harassing in nature.
CONSEQUENCES OF CONVERSION

This section is by the editor.

If a broker uses trust funds for any purpose not authorized by his client and not to his client’s direct benefit, then the broker is in violation of his fiduciary responsibilities as a licensee, an agent, and as a trustee – a violation known as “trust fund conversion.”

Examples of conversion range from sloppy record keeping to felonious embezzlement.

Certainly the use of an advance fee as stake for a poker game would be an egregious and obvious example of conversion but so would be the broker’s innocent failure to keep records to document how he honestly spent a client’s advance fee.

The broker who converts trust funds faces sanctions from the Commissioner, his client, the IRS, and the district attorney.

**Commissioner’s Sanctions**

Never forget that the Commissioner serves not to protect licensees but rather to protect the public from licensees (BPC §10050). The Commissioner is especially attentive to trust fund violations.

Should the Commissioner believe a broker is or has converted trust funds, the Commissioner may suspend the broker’s license and petition the Superior Court for injunctive relief including: 1) an order to desist, 2) a claim for restitution (BPC §10081), and 3) the appointment of a receiver. Should a receiver be appointed he is empowered as an officer of the Court to assume the full powers of a trustee. Should the receiver find it necessary to protect trust funds, he may even file bankruptcy on the broker’s behalf (BPC §10081, §10081.5).

To protect the public, the Audit Section of the BRE conducts hundreds of random audits each year. If in an audit, the Commissioner discovers the broker has converted more the $10,000, the Commissioner may suspend the broker’s license pending a formal hearing.

**Civil Liability Sanctions**

A broker may be sued by his client for converting trust funds. If the broker is found liable, his aggrieved client will be awarded damages, may be awarded any gain the broker may have realized in using the converted funds, and may even be awarded punitive damages if the trust funds were converted using fraud or with malice (CC §1153). Punitive damages may be three times the amount of recovery plus interest and attorneys fees. By statute, any misuse of trust funds by a broker is an abrogation of the broker’s fiduciary duty as an agent and therefore legally regarded as fraud (aka, “constructive fraud”).

By statute (BPC §10146.), the misuse of advance fees by a broker entitles his client to sue for treble damages and attorneys fees. Misuse includes the broker’s failure to adequately account for his use of a client’s advance fee.
Finally, the Commissioner may suspend or revoke the license of any broker found liable for trust fund conversion without the usual need to conduct an independent investigation.

A recent decision by the California Court of Appeals casts strong doubt on the above assertion. The Court in Grubb Company, Inc. v. Bureau of Real Estate, 2012 ruled that a finding of liability against a broker in a civil action could not be used by the Commissioner to justify his revocation of that broker’s license since the standard of proof in a civil action (“preponderance of the evidence”) is lower than the standard required by the Commissioner to deprive a broker of his livelihood (“clear and convincing proof”).

IRS Sanctions
The IRS requires that taxpayers report all income even income derived from an illegal source such as embezzled trust funds. Failure to report embezzled funds may result in fines and subject the broker to IRS’s special powers of seizure and garnishment.

If the amount is large and the broker may even be convicted of tax evasion and sent to prison.

Criminal Sanctions
By statute (Penal Code §506), conversion of trust funds is embezzlement if conducted using fraud or malice. Embezzlement is a felony offense punishable by fine and prison.

12 SAMPLE TRANSACTIONS

To demonstrate the record keeping requirements discussed in this course, we have simulated trust account records for typical real estate transactions occurring over a thirty-day period. To set the stage, let us assume that James Adams, a real estate broker, owns and operates a one-man real estate office specializing in residential sales and property management. Broker Adams has one trust fund bank account. We will look at the trust account activity for this office for the month of May, 2000.

The use of columnar records to record these transactions is illustrated in Exhibits 1-10 at the end of this course. As previously discussed, a broker may use other types of records as long as they meet generally accepted accounting standards.

2000 TRANSACTIONS

May 1  Opened a trust account with First County Bank and deposited $100 of his own money to cover bank service charges.

May 1  Entered into agreements to manage the following rental properties:
May 3 Deposited the following rents received from tenants of managed properties:

<table>
<thead>
<tr>
<th>Property</th>
<th>Tenant’s Name</th>
<th>Rent Received</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. 1538 South Ave.</td>
<td>B. Harris</td>
<td>$600</td>
</tr>
<tr>
<td>b. 3490 Tower St., Unit 1</td>
<td>R. Robertson</td>
<td>350</td>
</tr>
<tr>
<td>c. 2351 Kingston Way</td>
<td>I. Warren</td>
<td>450</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$1,400</td>
</tr>
</tbody>
</table>

May 5 Received a $2,000 check payable to broker from Mr. and Mrs. Dennis White as deposit for their offer to buy a house at 615 Lake Drive, Anycity, owned by Mr. and Mrs. Richard J. Jensen. Buyers’ offer instructed broker to hold the check uncashed until their offer was accepted by the Jensens.

May 5 Received and deposited $750 from T. Sundance representing rent of $500 for September 5 to 30, and $250 security deposits for 7365 Meadow Circle.

May 5 Was notified by the Jensen’s that they accepted the offer on their property.

May 6 Deposited the $2,000 check from Mr. and Mrs. White.

May 8 Obtained an exclusive listing to sell a six-plex at 915 Galaxy St., Anycity, owned by R. Jays.

May 9 Received $1,000 from W. Allen, owner of 9152 High Way, to cover anticipated expenses for the property. Amount was deposited the same day.

May 10 Issued the following checks to pay for various expenses connected with the managed properties:

<table>
<thead>
<tr>
<th>Payee</th>
<th>Purpose</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1001</td>
<td>ABC Mortgage Co. Mortgage payment for 1538</td>
<td>$450</td>
</tr>
<tr>
<td></td>
<td>South Ave.</td>
<td></td>
</tr>
<tr>
<td>1002</td>
<td>Anycity Treasury Utilities for 1538 South</td>
<td>35</td>
</tr>
<tr>
<td></td>
<td>Ave.</td>
<td></td>
</tr>
<tr>
<td>1003</td>
<td>Professional Cleaners Cleaning for 3490</td>
<td>25</td>
</tr>
<tr>
<td></td>
<td>Tower St.</td>
<td></td>
</tr>
<tr>
<td>1004</td>
<td>Mr. Handyman Minor repairs on 2351 Kingston</td>
<td>25</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>$565</td>
</tr>
</tbody>
</table>

May 14 Received a $4,000 check from B. Sun, payable to Title Escrow Company, with an offer to buy the 915 Galaxy property.

May 15 Received R. Jays’ acceptance of the buyer’s offer on 915 Galaxy Street.

May 16 Delivered the $4,000 check from B. Sun to Title Escrow Company.
May 19  Issued check number 1005 for $2,000 to First Title Co. for account of Mr. and Mrs. White, buyers of the 615 Lake Drive property.

May 22  Received an offer and a $3,000 check as deposit from R. Olive to buy a single family house at 31009 Technology Street owned by T. Evans.

May 24  Returned R. Olive’s check after seller rejected the offer.

May 31  Charged property management fees to the following accounts and issued check number 1006 for $330 payable to himself:

<table>
<thead>
<tr>
<th>Property Owner</th>
<th>Management Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>T. Eddie</td>
<td>$45</td>
</tr>
<tr>
<td>L. Stewart</td>
<td>100</td>
</tr>
<tr>
<td>W. Allen</td>
<td>80</td>
</tr>
<tr>
<td>S. Manly</td>
<td>60</td>
</tr>
<tr>
<td>J. Bird</td>
<td>45</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$330</strong></td>
</tr>
</tbody>
</table>

May 31  Sent statement of account to each owner of the managed properties.

13  **BACKGROUND INFORMATION**

James Adams keeps four types of columnar records:

1. Bank Account Record [#4522]. This record is required under BRE Reg. 2831 for each trust account a broker has.

2. Record of Undeposited Receipts [#4524]. This is required under BRE Reg. 2831.

3. Separate Beneficiary Record [#4523]. This is required under BRE Reg. 2831.1.

4. Separate Property Record [#4525]. This serves the same purpose as the Separate Beneficiary Record [#4523].

To illustrate the recording process, listed below are the entries made on the books by James Adams as well as the documents prepared or obtained as support for each transaction. The actual entries are shown on the forms/exhibits at the end of this course.

Note that:

- Each entry to any record shows all the pertinent information of the transaction, such as the date, name of payee, name of payor, amount, check number, etc.

- The daily bank balance is computed and posted on the Bank Account Record [#4522] after recording the transactions.

- The balance owing to the client is computed and posted on the Separate Beneficiary Record [#4523] or Separate Property Record [#4525], after posting transactions.
Trust Funds, 2nd Edition

- Any entry made on the Bank Account Record [#4522] has a corresponding entry on a Separate Beneficiary Record [#4523] or a Separate Property Record [#4525], and vice versa.

- All records except the Record of Undeposited Receipts [#4524] show entries in chronological sequence regardless of transaction type. The Record of Undeposited Receipts [#4524] shows the disposition of a trust fund in the same line as the receipt is entered, rather than in chronological sequence.

14  **STEP-BY-STEP NARRATIVE**

(Actual recording shown on Exhibits 1-10 at end of this course.)

<table>
<thead>
<tr>
<th>Date</th>
<th>Documentation</th>
<th>Entries</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 1</td>
<td>Deposit slip prepared by broker.</td>
<td>Record the deposit on:&lt;br&gt;1. The Bank Account Record. Balance is $100. (Exh. 1)&lt;br&gt;2. A newly prepared Separate Beneficiary for James Adams. Balance is $100. (Exh. 2)&lt;br&gt;No entries needed since nothing of value was received and because there were no changes to the trust fund balance.</td>
</tr>
<tr>
<td>May 1</td>
<td>Management agreements signed by property owners and broker.</td>
<td>Record the $1,400 receipt on:&lt;br&gt;1. The Bank Account Record. New balance is $1,500 (Exh. 1)&lt;br&gt;2. Newly prepared Separate Beneficiary Records for:&lt;br&gt;   T. Eddie – balance is $600 (Exh. 4)&lt;br&gt;   L. Stewart – balance is $350 (Exh. 5)&lt;br&gt;   S. Manly – balance is $450 (Exh. 6)&lt;br&gt;Enter transaction on the Record of Undeposited Receipts. (Exh. 3)&lt;br&gt;No Separate Beneficiary Record is necessary since the check was not deposited.</td>
</tr>
<tr>
<td>May 3</td>
<td>Collection receipts Nos. 2, 3, and 4 issued to B. Harris, R. Robertson, and I. Warren respectively.</td>
<td>Record the $750 deposit on:&lt;br&gt;1. The Bank Account Record. (Exh. 1)&lt;br&gt;2. Newly prepared Separate Beneficiary Records for:&lt;br&gt;   J. Bird – Sundance’s Security Deposit, balance is $250. (Exh. 7)&lt;br&gt;   J. Bird – balance is $500. (Exh 8)&lt;br&gt;(Note: Since security deposits will be accounted to the tenant in the future, James Adams, keeps a separate record for deposits (Exh.’s 7&amp;8). Total liability to the owner, J. Bird, is the sum of the two records – one for security deposits, another for rents and other transactions.)</td>
</tr>
<tr>
<td>May 5</td>
<td>Real Estate Purchase Contract and Receipt for Deposit signed by Mr. and Mrs. White Collection receipt No. 1 issued to the White’s.</td>
<td>Record the $750 deposit on:&lt;br&gt;1. The Bank Account Record. (Exh. 1)&lt;br&gt;2. Newly prepared Separate Beneficiary Records for:&lt;br&gt;   J. Bird – Sundance’s Security Deposit, balance is $250. (Exh. 7)&lt;br&gt;   J. Bird – balance is $500. (Exh 8)&lt;br&gt;(Note: Since security deposits will be accounted to the tenant in the future, James Adams, keeps a separate record for deposits (Exh.’s 7&amp;8). Total liability to the owner, J. Bird, is the sum of the two records – one for security deposits, another for rents and other transactions.)</td>
</tr>
<tr>
<td>May 5</td>
<td>Collection receipt No. 5 issued to T. Sundance. Receipt showed that $500 of the $750 was for rent and the other $250 was for security deposit.</td>
<td>Record $2,000 deposit on:&lt;br&gt;1. Bank Account record. New balance is $4,250 (Exh. 1)&lt;br&gt;2. A newly prepared Separate Beneficiary Record – Mr.</td>
</tr>
</tbody>
</table>
May 8
Exclusive Listing Agreement signed by sellers and broker.

May 9
Collection receipt No. 6 issued to W. Allen.

May 10
Checks issued by broker. Supporting papers for each check.

May 14
Real Estate Purchase Contract and Receipt for $4,000 deposit signed by B. Sun.

May 15
Real Estate Purchase Contract and Receipt for Deposit signed by R. Jays.

May 16
Receipt issued by Title Escrow Company.

May 19
Check for $2,000 issued by broker. Receipt issued by First Title Company.

May 22
Real Estate Purchase Contract and receipt for Deposit signed by R. Olive.

May 24
Real Estate Purchase Contract and Receipt for Deposit rejected by T. Evans.

May 31
List showing the breakdown of the check amount, showing the charge to each owner.

(Note: A list is necessary as support for a check disbursement chargeable to a number of beneficiaries. Posting the entries on the separate records without such a list is not sufficient.)

And Mrs. White/Mr. and Mrs. Jensen. Account balance is $2,000. (Exh. 9)

3. Record of Undeposited Receipts. (Exh. 3) Shows disposition of check previously entered on the record.

Record receipt on:
1. The Bank Account Record. New balance is $5,250. (Exh. 1)
2. A newly prepared Separate Beneficiary Record – W. Allen. Balance is $1,000. (Exh. 10)

Record disbursements on:
1. Bank Account Record. New Balance is $4,685 (Exh. 1)
2. Separate Beneficiary Records for:
   T. Eddie – Balance (1001, 1002) now $110. (Exh. 4)
   L. Stewart – Balance now $295. (Exh. 5)
   S. Manley – Balance now $425. (Exh. 6)

Record receipt on the Record of Undeposited Receipts. (Exh. 3)

No entry was needed since there was no receipt or disbursement of funds.

Note disposition of check on the Record of Undeposited Receipts. (Exh. 3)

Record disbursements on the:
1. Bank Account Record. New balance is $2,685. (Exh. 1)
2. Separate Beneficiary Record – Mr. and Mrs. White/Mr. And Mrs. Jensen. New balance is $0. (Exh. 9)

Record receipt on the Record of Undeposited Receipts. (Exh. 3)

Post the return of check on the Record of Undeposited Receipts. (Exh. 3)
(Note: No new record is created. The 05/22 record’s “Disposition of Funds” and “Date of Disposition” columns are posted with the values “Returned to Buyer” and “05/24” respectively.)

Record disbursements on the:
1. Bank Account Record. New balance is $2,685. (Exh. 1)
2. Separate Beneficiary Records for:

<table>
<thead>
<tr>
<th>New Owners</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>T. Eddie</td>
<td>$70</td>
</tr>
<tr>
<td>L. Stewart</td>
<td>$195</td>
</tr>
<tr>
<td>W. Allen</td>
<td>$920</td>
</tr>
<tr>
<td>S. Manley</td>
<td>$365</td>
</tr>
<tr>
<td>J. Bird</td>
<td>$455</td>
</tr>
</tbody>
</table>

After recording the daily transactions, the next step in the trust fund accounting process is the reconciling of records at the end of the month. James Adams prepared reconciliation schedules by comparing the bank
balance on the Bank Account Record [#4522] with the bank statement balance (the bank reconciliation) and also with the total of the Separate Beneficiary Records [#4523] balances (the reconciliation report).

The bank statement and reconciliations are shown on the next two pages.
## Trust Funds, 2nd Edition

**FIRST COUNTY BANK**

**MAIN BRANCH**
5 Main Avenue
ANYCITY, CA 90002

**STATEMENT**

**DATE OF THIS STATEMENT 05/31/00**

JAMES ADAMS
TRUST ACCOUNT
8310 ORANGE AVENUE
ANYCITY, CA 90002
CUSTOMER SINCE 1995

**CHECKING ACCT. 123456**

**SUMMARY: PREVIOUS STATEMENT BALANCE ON 04/30/00 .......................................................... 00.00**

**TOTAL OF 5 DEPOSITS FOR ........................................................................................................ 5,250.00**

**TOTAL OF 4 CHECKS FOR ........................................................................................................ 2,540.00**

**TOTAL OF 1 OTHER DEBIT FOR .............................................................................................. 7.00**

**STATEMENT BALANCE ON 05/31/00 ..................................................................................... 2,703.00**

<table>
<thead>
<tr>
<th>CHECKS/ CHECKS</th>
</tr>
</thead>
<tbody>
<tr>
<td>OTHER DEBITS</td>
</tr>
<tr>
<td>CHECK NUMBER</td>
</tr>
<tr>
<td>1001</td>
</tr>
<tr>
<td>1002</td>
</tr>
<tr>
<td>1003</td>
</tr>
<tr>
<td>1005</td>
</tr>
</tbody>
</table>

| OTHER DEBITS    |
| DATE POSTED    | AMOUNT |
| 05/31          | SERVICE CHARGE 7.00 |

<table>
<thead>
<tr>
<th>DEPOSITS/ DEPOSITS</th>
</tr>
</thead>
<tbody>
<tr>
<td>OTHER CREDITS</td>
</tr>
<tr>
<td>DATE POSTED</td>
</tr>
<tr>
<td>5/1</td>
</tr>
<tr>
<td>5/5</td>
</tr>
<tr>
<td>5/6</td>
</tr>
<tr>
<td>5/9</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>DAILY BALANCE</th>
<th>DATE</th>
<th>AMOUNT</th>
<th>DATE</th>
<th>AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>5/1</td>
<td>100.00</td>
<td>5/14</td>
<td>4,800.00</td>
<td></td>
</tr>
<tr>
<td>5/5</td>
<td>2,250.00</td>
<td>5/16</td>
<td>4,710.00</td>
<td></td>
</tr>
<tr>
<td>5/6</td>
<td>4,250.00</td>
<td>5/21</td>
<td>2,710.00</td>
<td></td>
</tr>
<tr>
<td>5/9</td>
<td>5,250.00</td>
<td>5/31</td>
<td>2,703.00</td>
<td></td>
</tr>
</tbody>
</table>
Trust Funds, 2nd Edition

James Adams
Bank Reconciliation
First County Bank
May 31, 2000

Balance per bank statement, 5/31/00 ................................................................. $2,703.00
Add deposits in transit ........................................................................................................... -0-
Less outstanding checks:
check #1004 ................................................................. $25.00
#1006 ........................................................................... 330.00 <355.00>
Adjusted bank balance, 5/31/00 ..................................................................................... $2,348.00
Balance per books, 5/31/00 ............................................................................................. $2,355.00
Less May bank service charge ......................................................................................... <7.00>
Adjusted balance, 5/31/00 ............................................................................................... $2,348.00

James Adams
Reconciliation Report
First County Bank
Account No. 123456
May 31, 2000

<table>
<thead>
<tr>
<th>Beneficiary</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>James Adams (Broker)</td>
<td>$93.00</td>
</tr>
<tr>
<td>W. Allen</td>
<td>920.00</td>
</tr>
<tr>
<td>J. Bird</td>
<td>250.00</td>
</tr>
<tr>
<td>J. Bird</td>
<td>455.00</td>
</tr>
<tr>
<td>T. Eddie</td>
<td>70.00</td>
</tr>
<tr>
<td>S. Manly</td>
<td>365.00</td>
</tr>
<tr>
<td>L. Stewart</td>
<td>195.00</td>
</tr>
<tr>
<td>Total per subsidiary records</td>
<td>$2,348.00</td>
</tr>
</tbody>
</table>

(Agrees with bank account record balance.)

15 Questions and Answers

Q. Are security deposits on rental units the property of the owner or should they be held in trust by the broker for the tenant?
A. They are trust funds. As such, control and disbursement of the security deposits are at the instruction of the property owner.

Q. Am I permitted to wait until checks deposited to my trust account have cleared before I issue a trust check to fund a customer’s check?
A. Although the Real Estate Law is silent on this, good business practice dictates that you wait until a customer’s check deposited to your trust account has cleared prior to the issuing of your trust check as a refund.

Q. How should I handle an earnest money check which is to be deposited into escrow upon acceptance of the offer?
A. Such a check may be held until the offer is accepted and then placed in escrow but only when directed to do so by the buyer, provided you disclose to the seller the fact the check is being held in uncashed form. In such cases, it is good practice to include such a provision in the deposit receipt. You must keep a columnar record of the receipt of the check, the name of the escrow company, and the date the check was forwarded to the escrow.

Q. As a broker-owner of rentals, do I have to put security deposits in a trust account?
A. Money you receive on your own property is received as a principal, not as an agent. As such, these are not trust funds and should not be placed in the trust account.

Q. Must I keep a deposit receipt signed only by the buyer and rejected by the seller?
A. Yes. Such a record must be maintained for three years.

Q. May I maintain one trust fund account for both collections from my property management business and deposits on real estate sales transactions?
A. Since property management funds usually involve multiple receipt of funds and several monthly disbursements, it is suggested that separate trust fund accounts be maintained for property management funds and earnest money deposits. However, all trust funds can be placed in the same trust fund account as long as separate records for each trust fund deposit and disbursement are maintained properly and the account is not an interest-bearing account.

Q. If the buyer and seller decide to go directly to escrow and the buyer makes out a check to the escrow company and hands it directly to the escrow clerk, do I have to maintain any records of this check?
A. No. You must maintain records only of trust funds which pass through your hands for the benefit of a third party.

Q. How long must I keep deposit receipts?
A. Deposit receipts must be maintained for three years.

16  SUMMARY

We might say this course presents the three R's of trust funds: Responsibility, Requirements, and Records.

It is a real estate broker’s responsibility to protect clients’ funds at all times and keep clients fully informed of the nature and disposition of all trust funds.

To aid brokers in carrying out this responsibility, the Real Estate BRE Regulations include requirements concerning trust funds. A real estate broker also needs to meet other requirements from a practical business point of view. To protect clients’ funds adequately and in the business-like fashion expected, the broker must keep accurate records.
### Exhibit 1: Bank Account Record

<table>
<thead>
<tr>
<th>Date Received</th>
<th>From Whom Received or To Whom Paid</th>
<th>Description</th>
<th>Amount Received</th>
<th>Reference</th>
<th>Date of Deposit</th>
<th>Date of Pay Out</th>
<th>Amount Paid Out</th>
<th>Check Number</th>
<th>Date of Check</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-10</td>
<td>James Adams</td>
<td>Open TA Account</td>
<td>$100.00</td>
<td>#10</td>
<td>5-10</td>
<td></td>
<td>$100.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-3</td>
<td>B. Harris</td>
<td>Rent: 1538 South Av.</td>
<td>$600.00</td>
<td>#2</td>
<td>5-3</td>
<td></td>
<td>$700.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-3</td>
<td>R. Robertson</td>
<td>Rent: 3490 Tower #1</td>
<td>$350.00</td>
<td>#3</td>
<td>5-3</td>
<td></td>
<td>$1,050.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-3</td>
<td>L. Warren</td>
<td>Rent: 2351 Kingston Way</td>
<td>$450.00</td>
<td>#4</td>
<td>5-3</td>
<td></td>
<td>$1,500.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-5</td>
<td>T. Sundance</td>
<td>Rent: $500, Dep. $250</td>
<td>$750.00</td>
<td>#5</td>
<td>5-5</td>
<td></td>
<td>$2,500.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-5</td>
<td>Mr. &amp; Mrs. Dennis White</td>
<td>Dep.: 615 Lake Dr.</td>
<td>$2,000.00</td>
<td>#6</td>
<td>5-6</td>
<td></td>
<td>$4,250.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-9</td>
<td>W. Allen</td>
<td>Owner Contribution</td>
<td>$1,000.00</td>
<td>#6</td>
<td>5-9</td>
<td></td>
<td>$5,250.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-9</td>
<td>ABC Mortgage Co.</td>
<td>Neg. Rent: 1538 South Av</td>
<td>$450.00</td>
<td>1001</td>
<td>5-10</td>
<td></td>
<td>$4,800.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-9</td>
<td>Any city Treasury</td>
<td>Utilities: 1538 South Av</td>
<td>$35.00</td>
<td>1002</td>
<td>5-10</td>
<td></td>
<td>$4,965.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-9</td>
<td>Professional Cleaners</td>
<td>Cleaning: 3490 Tower #1</td>
<td>$55.00</td>
<td>1003</td>
<td>5-10</td>
<td></td>
<td>$4,910.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-9</td>
<td>Mr. Handyman</td>
<td>Repairs: 2351 Kingston Way</td>
<td>$25.00</td>
<td>1004</td>
<td>5-10</td>
<td></td>
<td>$4,895.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-19</td>
<td>First Title Co.</td>
<td>Deposit: 615 Lake Dr.</td>
<td>$2,000.00</td>
<td>1005</td>
<td>5-19</td>
<td></td>
<td>$2,685.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Mgmt. Fees: see schedule</td>
<td>$320.00</td>
<td>1006</td>
<td>5-30</td>
<td></td>
<td>$2,335.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>First County Bank</td>
<td>May Bank Service Charge</td>
<td>$7.00</td>
<td>DM</td>
<td>5-31</td>
<td></td>
<td>$2,348.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Exhibit 2: Separate Beneficiary Record [#4523]

<table>
<thead>
<tr>
<th>Description</th>
<th>Discharge of Trust Accountability for Funds Paid Out</th>
<th>Trust Accountability for Funds Received</th>
<th>Account Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Open TA Account</td>
<td>Date of Check</td>
<td>Check Number</td>
<td>Amount</td>
</tr>
<tr>
<td>May '00 Service Chg</td>
<td>5-31</td>
<td>CM</td>
<td>7.00</td>
</tr>
</tbody>
</table>

RE 4523 (Rev. 2/94)

### Exhibit 3: Record of Undeposited Receipts [#4524]

<table>
<thead>
<tr>
<th>Date Received</th>
<th>Form of Receipt</th>
<th>Amount</th>
<th>Received From</th>
<th>Description of Property or Other Identification</th>
<th>Direction of Funds (To accrue, principal, trust account, or returned)</th>
<th>Date of Disposition</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-5-00</td>
<td>check</td>
<td>2,000**</td>
<td>Mr. &amp; Mrs. Dennis White</td>
<td>615 Lake Drive</td>
<td>To Trust Account Upon Acceptance</td>
<td>5-6-00</td>
</tr>
<tr>
<td>5-14</td>
<td>check</td>
<td>4,000**</td>
<td>B. Sun</td>
<td>915 Galaxy</td>
<td>To Title Escrow Company</td>
<td>5-16</td>
</tr>
<tr>
<td>5-22</td>
<td>check</td>
<td>3,000**</td>
<td>R. Olive</td>
<td>31009 Technology St</td>
<td>Returned to Buyer</td>
<td>5-24</td>
</tr>
</tbody>
</table>

RE 4524 (Rev. 2/99)
### Exhibit 4: Separate Property Record

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No.</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Disbursed</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-3-00</td>
<td>B. Harris</td>
<td>Rent-May 00</td>
<td>#2</td>
<td>600.00</td>
<td>5-3-00</td>
<td></td>
<td>600.00</td>
</tr>
<tr>
<td>5-10</td>
<td>ABC Mortgage Co.</td>
<td>Mortgage Payment</td>
<td>1001</td>
<td></td>
<td>450.00</td>
<td>150.00</td>
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</tr>
<tr>
<td>5-10</td>
<td>Any City Treasury</td>
<td>Utilities</td>
<td>1002</td>
<td></td>
<td>35.00</td>
<td>115.00</td>
<td></td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Management Fee</td>
<td>1006</td>
<td></td>
<td>45.00</td>
<td>70.00</td>
<td></td>
</tr>
</tbody>
</table>

### Exhibit 5: Separate Property Record

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No.</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Disbursed</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-3-00</td>
<td>R. Robertson</td>
<td>Rent-May 00</td>
<td>#3</td>
<td>350.00</td>
<td>5-3-00</td>
<td></td>
<td>350.00</td>
</tr>
<tr>
<td>5-16</td>
<td>Professional Cleaners</td>
<td>Cleaning</td>
<td>1003</td>
<td></td>
<td>55.00</td>
<td>295.00</td>
<td></td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Management Fee</td>
<td>1006</td>
<td></td>
<td>100.00</td>
<td>19.50</td>
<td></td>
</tr>
</tbody>
</table>

---

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### Exhibit 6: Separate Property Record [#4525]

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Disbursed</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-3-00</td>
<td>J. Warren</td>
<td>Rent-May 00</td>
<td>#4</td>
<td>450.00</td>
<td>5-3-00</td>
<td></td>
<td>450.00</td>
</tr>
<tr>
<td>5-10</td>
<td>Mr. Handyman</td>
<td>Repairs</td>
<td>1004</td>
<td></td>
<td></td>
<td>25.00</td>
<td>425.00</td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Management Fee</td>
<td>1006</td>
<td></td>
<td></td>
<td>60.00</td>
<td>365.00</td>
</tr>
</tbody>
</table>

**RE: 4525 (Rev. 2/94)**

### Exhibit 7: Separate Property Record [#4525]

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Disbursed</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-5-00</td>
<td>T. Sundance</td>
<td>Deposit</td>
<td>#5</td>
<td>250.00</td>
<td>5-5-00</td>
<td></td>
<td>250.00</td>
</tr>
</tbody>
</table>

**RE: 4525 (Rev. 2/94)**
### Exhibit 8: Separate Property Record [#4525]

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No.</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Deposited</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-5-00</td>
<td>T. Sundance</td>
<td>Rent - May 2000</td>
<td>#5</td>
<td>500.00</td>
<td>5-5-00</td>
<td>500.00</td>
<td>500.00</td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Management Fees</td>
<td>1006</td>
<td></td>
<td>45.00</td>
<td>455.00</td>
<td></td>
</tr>
</tbody>
</table>

### Exhibit 9: Separate Beneficiary Record [#4523]

**Identification of Transaction (names, addresses, account numbers, etc.)**

Mr. & Mrs. White/Mr. & Mrs. Jensen

RE: 615 Lake Drive, Any City

<table>
<thead>
<tr>
<th>Description</th>
<th>Discharge of Trust Accountability For Funds Paid Out</th>
<th>Trust Accountability For Funds Received</th>
<th>Account Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase Deposit</td>
<td>Date of Check</td>
<td>Check Number</td>
<td>Amount</td>
</tr>
<tr>
<td>Deposit to Title Co.</td>
<td>5-19-00</td>
<td>1005</td>
<td>2,000.00</td>
</tr>
</tbody>
</table>
### Exhibit 10: Separate Property Record [#4525]

<table>
<thead>
<tr>
<th>Date</th>
<th>Received From or Paid To</th>
<th>Description</th>
<th>Receipt/Check No</th>
<th>Amount Received</th>
<th>Date Deposited</th>
<th>Amount Disbursed</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-9-00</td>
<td>W. Allen</td>
<td>Owner Contribution</td>
<td>#5 1,000.00</td>
<td>5-9-00</td>
<td></td>
<td></td>
<td>1,000.00</td>
</tr>
<tr>
<td>5-31</td>
<td>James Adams</td>
<td>Management Fees</td>
<td>1006</td>
<td></td>
<td>80.00</td>
<td></td>
<td>920.00</td>
</tr>
</tbody>
</table>

RII 4525 (Rev. 2/94)