Date of Hearing: March 18, 2025

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Avelino Valencia, Chair
AB 493 (Harabedian) – As Amended March 10, 2025

SUBJECT: Property insurance notice of cancellation

SUMMARY: Starting January 1, 2026, financial institutions are required to pay interest to the borrower for insurance proceeds following property damage or loss held in escrow. Applies this requirement to loans executed before January 1, 2026 to specified properties impacted by the January 2025 Los Angeles-area wildfires.

Specifically, **this bill**:

1) Starting January 1, 2026, financial institutions that make mortgage loans are required to pay at least 2% interest on amounts received in advance for payment of insurance proceeds following property damage or loss, or other purposes related to the property.

2) Provides that for loans executed before January 1, 2026, the provisions of the bill only apply if the property securing the loan is located within a federally or state-declared disaster area and directly impacted due to the wildfires in the Counties of Los Angeles and Ventura subject to the state of emergency declared by the Governor on January 7, 2025.

3) States this change shall not be construed to unreasonably impair the terms of those loans, and its provisions are intended solely to ensure equitable treatment of borrowers whose escrowed funds are held for property-related expenses.

4) Includes findings and declarations that the change is deemed necessary due to the urgent need to protect wildfire-impacted borrowers in Los Angeles and Ventura Counties and that this bill aims to guarantee that escrowed insurance payouts earn the same interest as funds held for taxes or other property-related expenses.

EXISTING LAW:

1) Requires financial institutions that make mortgage loans to pay at least 2% interest on amounts received in advance for payment of taxes and assessments on the property, insurance, or other purposes related to the property. (Civil Code Section 2954.8)

2) Requires the Department of Financial Protection and Innovation (DFPI) to license and regulates escrow agents under the Escrow Law (Financial Code Section 17000 et seq.).

3) Requires residential mortgage lenders and mortgage loan servicers to be licensed under the California Residential Mortgage Lending Act (CRMLA) which regulates mortgage banking activities. (Financial Code Section 50000 et seq.)

FISCAL EFFECT: Unknown. This bill is keyed Fiscal by Legislative Counsel.

COMMENTS:

1) Purpose

According to the author:

Current California law requires lenders to pay interest on escrowed funds for property taxes, mortgage insurance, and homeowners insurance premiums, but it does not extend this requirement to insurance payouts after disasters. When a homeowner receives an insurance payout following a wildfire or other disaster, lenders often hold these funds in escrow, earning interest while the homeowner waits to rebuild. However, unlike other escrowed funds, there is no legal requirement for lenders to pass that interest on to homeowners. AB 493 closes this loophole by ensuring homeowners receive the interest earned on their insurance payouts, just as they do with other escrowed property funds.

2) Background:

a) Los Angeles wildfires.

California has faced an alarming increase in destructive wildfires. Most of the largest and devastating fires have taken place within the last decade, culminating in a particularly severe outbreak in recent years. This period has witnessed some of the worst wildfires in the state's recorded history.

More recently, January 2025 wildfires, often referred to as firestorms due to the intense hurricane-force winds that helped the fires quickly spread, destroyed more than 16,000 structures and has led to widespread hardship for victims and the surrounding communities. According to an analysis by the Los Angeles Times, real estate losses from the two largest fires – Palisades and Eaton – could exceed $30 billion, and the fires caused the displacement of approximately 13,000 households.

According to the CA Department of Insurance, LA County Wildfire Claims Tracker, updated February 5, 2025[1]:

- 33,717 claims have been filed.
- 19,854 claims have been partially paid.
- $6.9 billion claims have been paid to date.

b) Escrow Accounts and Insurance Payouts

An escrow account for insurance claims is a temporary financial account used to hold insurance payout funds, ensuring they are properly used for property repairs. This is commonly required in homeowners insurance claims, especially when the property has a mortgage. Instead of paying the homeowner directly, the insurer deposits the funds into an escrow account managed by the mortgage lender or a third-party administrator.

[1] https://www.insurance.ca.gov/01-consumers/180-climate-change/Wildfire-Claims-Tracker.cfm

While the terms of each policy is different, here is a general description of the steps involved in the escrow process. After the claim is approved, funds are placed in escrow rather than given directly to the homeowner. The lender then releases payments in stages as repairs progress, ensuring the work is completed properly and contractors are paid. Once the final repairs are inspected and verified, the remaining balance is released to the homeowner or contractor. This prevents misuse of funds and ensures the property is restored.

Escrow accounts protect lenders by ensuring their collateral (the home) is properly repaired. However, if a property does not have a mortgage or if the claim is small, insurers typically pay the homeowner directly without requiring escrow.

3) <u>Gray v. Quicken Loans, Inc. (2021) 62 Cal.App.5th 920</u>

In 2017, William Gray had his home destroyed in the Thomas Fire in Ventura, California. Mr. Gray's hazard insurance policy issued a payout of $1,342,740, which was jointly paid to him and his mortgage lender, Quicken Loans, Inc. According to the Deed of Trust, Quicken was allowed to hold the insurance proceeds in escrow and disburse them as the home was being repaired. Quicken did not pay interest on these funds while they were held in escrow. Mr. Gray sued arguing that Civil Code Section 2954.8 requires Quicken to pay 2% interest per year on insurance proceeds held in escrow. The California Court of Appeals affirmed the trial court ruling that Quicken had no obligation to pay interest on insurance proceeds.

The Appellate Court based its decision on the findings in Lippitt v. Nationstar Mortgage, LLC (Lippitt)[2]:

> Based upon the statutory and contractual language, we agree with Lippitt that section 2954.8 "applies to common escrows maintained to pay taxes, assessments, and insurance premiums -- not to the comparatively unique example of hazard insurance proceeds held by a lender pending property rebuilding." (Lippitt, supra, 2020 U.S. Dist. Lexis 122881, *21.)

AB 493 would add insurance proceeds that are held in an escrow account following property damage or loss to the purposes for which financial institutions are required to pay interest to borrowers.

<u>8) Author commitments and future refinement.</u>

The author commits to clarify that this bill applies to pre-January 1, 2026 loans only for insurance payouts that remain held in escrow on or after the effective date of this act. Additionally, that funds disbursed prior to the effective date are not subject to the interest requirement.

In consultation with Assembly Judiciary, this clarification would help affirm that this bill is intended as a prospective measure governing the ongoing handling of funds, rather than impairing past transactions.

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[2] (Lippitt v. Nationstar Mortgage, LLC C.D.Cal. Apr.16, 2020, No. SA CV 19-1115-DOC-DFM) 2020 U.S. Dist. Lexis 122881

4) Urgency Clause

The author is requesting to adopt an urgency clause. Due to timing, the urgency clause will be adopted in Assembly Appropriations Committee.

REGISTERED SUPPORT / OPPOSITION:

Support

None received.

Opposition

None received.

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