

# RED FLAGS ON A PRELIMINARY REPORT

A Preliminary Report will often times reveal the existence of certain matters that could raise a red flag and as a result could delay the closing of escrow. Below are some potential matters that could show up on a Preliminary Report.

**TAXES:** These are standard. This is to show you the status of the taxes for the current tax year and/or any prior years that may still be outstanding.

**RED FLAG:**

1. Postponed property taxes. This is a program put on by the State of California for senior, blind and disabled citizens. This program will allow the State to pay the taxes for the owner in a deferral program. A demand is needed to be ordered by the Escrow to pay back the State of California to pay off all the postponed property taxes.
2. Also, a recorded power to sell. This means that the County has started the process of foreclosing on back taxes existing on a parcel. It must be verified that the taxes have not sold at auction when this type of instrument is present in the chain of title.

**CC&R'S:** These are standard. The CC&R's should be provided to the buyer by the Escrow Company. The buyer should read these thoroughly, especially if improvements to the property are contemplated. Also, for Condominiums these are the bylaws for the Condominium Complex.

**RED FLAG:** Some CC&R's prohibit certain types of improvements. Also, some CC&R's, in a Condominium project, prohibit types of pets.

**EASEMENTS:** These are standard. These are used for various reasons. The most common Easement is for Public Utility companies to have access to transfer power, water, gas, etc. Also, they provide for the ability of the Utility Company to have access to be able to maintain their public utilities within the property. Other Easements are for access rights

for multiple owners for various reasons (ingress, egress, landscaping, etc.).

**RED FLAG:** If improvements are contemplated (such as construction of a pool or spa, for example), then the buyer should request the easements to be plotted on a map to determine that there will not be any interference to contemplated improvements. Sometimes a survey may need to be obtained to determine exact locations of the easements. Removal of Easements can be a difficult process.

**COVENANT AND AGREEMENTS:** These are common. These are typically used when there is a mutual agreement with a City body and the owner of the property when there is a development or improvement to a property. The Agreements will bind the owner and future owners to certain actions. A copy of the Covenant and Agreement should be read. It is the buyer's responsibility to contact their own counsel if they do not understand how the Covenant and Agreement would affect them.

**RED FLAG:** Certain Covenant and Agreements will have permit requirements. Although, some Covenant and Agreements can be terminated with the City, the process is difficult.

**AGREEMENTS:** These are not common. Typically they are for Road Maintenance Agreements or mutual Easement Agreements. The Agreements will bind the owner and future owners to certain actions. A Copy of the Agreement should be read. It is the buyer's responsibility to contact their own counsel if they do not understand how the agreement would affect them.

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# CON'T RED FLAGS ON A PRELIMINARY REPORT

**RED FLAG:** Certain Agreements provide for cost and responsibility to the maintenance of the Easement. The buyer should be aware of this.

**TRUST DEEDS:** These are common. This is the mortgage to the property. Sometimes there may be a second Trust Deed, like an equity line of credit. Typically, these are paid off through the closing process. After it has been paid the lender will issue a reconveyance to remove the Trust Deed from the public record as an existing debt.

**RED FLAG:** Old Deeds of Trust of record, from prior owners, could still be of record and have not been reconveyed. When this occurs extra research needs to occur. Research to see if it was paid off and it was just never reconveyed. When that happens an indemnity from the prior title company may have to be ordered. Sometimes old Deeds of Trust may have been paid by the owner who was in title at that time. However, it is common that a reconveyance was never issued. A Bond may have to be obtained from a bonding company to remove the Deed of Trust from the public record as an existing debt. Pursuant to the California Civil Code, these bonds must cover 2 times the amount of the value of the Deed of Trust and the cost for these type of bonds could cost anywhere from 1% to 3% depending on the bonding company's requirements.

**ENCROACHMENTS:** The title company may discover that there is an encroachment existing. A fence, a driveway, etc., could encroach onto someone else's property. This usually means that the policy of title insurance will have to be subject to the existing encroachment.

**RED FLAG:** Sometimes the Lender will not lend on a property with an existing encroachment without an additional endorsement being issued to them, giving them coverage against forced removal of the encroachment. The endorsements are issued on a case by case basis depending on the encroachment type.

**NOTICE OF VIOLATION:** These will sometimes be recorded by a City or County agency for various different issues; such as sub-standard conditions due to a non-permitted addition, a violation to the sub-division map-act or abatement procedures.

**RED FLAG:** These are always a red flag. Typically, a lender will not lend with these outstanding conditions. A release is required from the governmental agency who recorded it. Escrow (or the seller or the seller's representative) will usually have to deal directly with the appropriate agency to resolve these types of issues.

**JUDGMENTS:** Typically, these are for monetary law suits and at times it can be for support fees due to a former spouse for child support or spousal support.

**RED FLAG:** A lender will almost always want these types of liens cleared during the close of escrow. If not paid, the lender's Deed of Trust would be a secondary lien behind the judgment. Escrows will have to obtain a demand and release. The process to obtain a judgment and release can be lengthy.

**BANKRUPTCY:** Bankruptcies are not common nor standard.

**RED FLAG:** Open bankruptcies require that the debtor get permission from the court to sell or encumber the asset (the property) or take on any new debt. Chapter 7 and 13 bankruptcies are the most common found in a transaction. An order from the bankruptcy trustee will be required to close an escrow transaction. The trustee will sometimes require that a payment be made to the court at close. A Chapter 7 bankruptcy is a complete washout of dischargeable debts. A Chapter 13 is a reorganization of debt and, typically, a payment plan is formalized.

**NOTICE OF PENDING ACTION:** This is typically a court action against the property. This type of instrument is also known as a Lis Pendens.

**RED FLAG:** This means that someone has a lawsuit pending, pertaining to the property. A demand and withdrawal of the pending action is required to be recorded prior to the close of escrow. Sometimes an order expunging the Lis Pendens is needed to clear the matter.

**Contact your title representative or title officer for further assistance if you see one of these red flags on your Preliminary Report.**

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