

PRELIMINARY REPORTS IN REAL ESTATE TRANSACTIONS

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The use of a preliminary report is standard practice in any real estate transaction. Once the seller and buyer have signed a purchase agreement, the parties send the purchase agreement to the title company (which also typically serves as the escrow company) in order to open escrow. Several days after opening escrow, the title company will issue a preliminary report that identifies the property that is being sold and lists the various exceptions to any title policy that may be issued. Sellers and buyers typically rely on preliminary reports to disclose any defects or problems to title. The reliability of preliminary reports has been heavily contested in California cases, but a recent California case allows a buyer to rely on the preliminary report for the description of the property that the buyer is purchasing.

In the recent case of *Lee v. Fidelity National Title Insurance Company* (2010) 188 Cal.App. 4th 583, the California appellate court ruled that a buyer may rely upon the preliminary report to accurately describe the property being purchased by the buyer. California law has established a general principal that preliminary reports are simply an offer by the title company to issue a title insurance policy in conformity with a preliminary report, but that the preliminary report itself may not be relied upon by either the seller or the buyer. In fact, California Insurance Code Section 12340.11 states that a preliminary report “shall not be construed as, nor constitute, a representation as to the condition of title to real property but shall constitute a statement of the terms and conditions upon which the issuer is willing to issue its title policy, if such offer is accepted.” Therefore, there is a strong presumption under California law that neither sellers nor buyers can rely upon the contents of a preliminary report.

In the *Lee* case, Karen and Terry Lee entered into a purchase agreement to buy two parcels of real property in Solano County that were described as Assessor Parcel Numbers 042-230-090 (“APN 9”) and 042-230-220 (“APN 22”). The Lees opened escrow with the defendant Fidelity Title Insurance Company, which issued a preliminary report that identified the property address as both assessor parcel numbers, included a page setting forth a legal description, referenced unpaid taxes on both assessor parcel numbers as an exception to coverage and included a Solano County Assessor’s Parcel Map with arrows pointing to both assessor parcel numbers. The Lees closed escrow in September, 1990 and their deed stated that a transfer tax had been paid for both assessor parcel numbers. From 1990 onward, the Lees paid property taxes on both assessor parcel numbers and from 1999 onward, they paid assessments charged by the reclamation district on both assessor parcel numbers.

In 2006, the Lees decided to sell their property and at that time, investigated the exact location of APN 22. Upon meeting with the Solano County Assessor, the assessor reviewed the legal descriptions and informed the Lees that the Walkers (the Lees’ neighbor) actually owned APN

22 and not the Lees. The assessor changed its tax records to reflect this change in ownership. At that point, the Lees retained an attorney and sent a letter to the defendant title company demanding that the defendant obtain clear title to APN 22 in favor of the Lees. Fidelity Title Company reviewed the case and rejected the Lees' claim on the basis that the legal description contained in the preliminary report only described APN 9 and not APN 22. Upon denying coverage, the Lees filed suit against the defendant to enforce the title policy. The trial court ruled in favor of the defendant and said that the Lees did not have a case because they did not have legal ownership of APN 22. The Lees appealed and the appellate court reversed the trial court and ruled in the Lees' favor.

The appellate court reasoned that the preliminary report offered to insure APN 22 by containing many references to APN 22, and including the Solano County Assessor's map with an arrow pointing to APN 22. The appellate court ruled that the Lees "could have reasonably expected, under the circumstances, that they were buying a title insurance policy on APN 22 that would conform to the preliminary report." The appellate court stated that Insurance Code Section 12340.11 supported this decision since preliminary reports are offers to insure the property that is identified in the preliminary report and the Lees' preliminary report specifically referenced APN 22.

The defendant title company countered that the legal description that was included with the preliminary report only described APN 9 and not APN 22. The appellate court conceded that this was correct but that the legal description was a metes and bounds description that could not be understood by an average person reading the preliminary report. Only a surveyor could understand a metes and bounds legal description, and the appellate court determined that purchasers were not required to obtain a surveyor to interpret a metes and bounds legal description in a preliminary report in order to confirm that this is actually the property that they are purchasing. The appellate court went on to state that any ambiguity created in the preliminary report between the legal description and the various references to APN 22 were created by the title company and not by the purchaser. Also, the court reasoned that it was the title company's responsibility, and not the purchaser's responsibility, to determine the correctness of the legal description to any property that it was going to insure. For these reasons, the appellate court ruled that the Lees reasonably relied on the preliminary report to describe the property that they thought they were purchasing, and therefore the title company was obligated to insure their title to APN 22.

This is an important case because many preliminary reports, especially for properties in agricultural areas, contain a metes and bounds legal description of the property. It is essential for any purchaser to know that their title insurance policy will cover the property that they think they are purchasing. Therefore, if a purchaser has any questions about a preliminary report or a legal description, the purchaser should talk with their real estate agent, the title company or a real estate attorney to address these concerns so that they do not find themselves in a situation similar to the Lees.

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