



Chapter 7



ESCROWS AND TITLE INSURANCE



I. ESCROWS IN GENERAL

Escrow

- Is created when a separate written agreement instructs a neutral third party to hold funds and only proceed when all the agreed to conditions have been performed

Escrow is:

- Highly recommended in all:
 - sales of real property
 - loans
 - exchanges
- Required by law in all:
 - liquor license transfers
 - security sales (impound accounts)
 - court-ordered transfers (such as probate sales)

A. Valid Escrow Requires:

REQUIREMENTS OF A VALID ESCROW

- 1. SIGNED ESCROW INSTRUCTIONS**
(FORM A BINDING CONTRACT BETWEEN BUYER AND SELLER)
- 2. NEUTRAL 3RD PARTY** (ESCROW COMPANY, ACTING AS A DUAL AGENT OF BUYER AND SELLER)
- 3. CONDITIONAL DELIVERY OF FUNDS AND DOCUMENTS** (WHEN ALL OF THE CONDITIONS IN THE ESCROW ARE MET)

REMEMBER THAT . . .

- * ESCROW INSTRUCTIONS ARE CONFIDENTIAL (BUYERS, SELLERS AND THEIR AGENTS)
- * AN ESCROW AGENT MUST BE STRICTLY IMPARTIAL AND MAY NOT GIVE ADVICE TO EITHER PARTY

B. Escrow Officer

- Not licensed by the state but an employee of a licensed escrow company
 - a neutral depository is an escrow business conducted by a licensed escrow holder
- Escrow officers (or “holder,” or “agent”) can also be:
 - Attorney - who performs escrow duties
 - Real Estate Broker - who handles escrows as part of their business

Duties of An Escrow Company

1. Conditional Delivery - delivery of all funds and documents when all conditions of escrow have been satisfied
2. Confidentiality - disclosure of any facts can be authorized only by the buyer or seller or their respective agents
3. Deposit Holder - must hold funds and documents until conditions are met and both parties have reached an agreement

Escrow sequence of events

1. Preliminary title search and report
2. Lender's demand (amount owed, pay-off statement, if any)
3. Request of new loan documents (if any)
4. Completion of conditions and depositing of funds
5. Adjustments and prorations
6. Transfer of existing fire policies or creation of new ones; fulfilling lender's terms for coverage and payee
7. Recording deed (closing date) and issuing of title insurance policy
8. Disbursement of funds
9. Escrow settlement statement sent to each party

Northern vs. Southern CA

- Delivery of signed escrow instructions
 - SC: bilateral escrow instructions are signed by principals just after start of escrow
 - NC: unilateral escrow instructions given to escrow officer just before close of escrow
- Who performs escrow services
 - SC: independent escrow companies (corporations) or financial institutions
 - NC: title insurance companies

Northern vs. Southern CA

- Who pays escrow fees
 - SC: split 50-50 between Buyer and Seller
 - NC: Buyer pays
- Who traditionally pays title insurance fees
 - SC: Seller pays CLTA standard policy
 - NC: Buyer pays CLTA standard policy
 - Both SC and NC, any coverage above CLTA coverage paid for by Buyer

C. Real Estate Brokers Can Conduct Escrows

- A broker can handle escrows for a fee only if the broker is acting as a real estate agent or principal in that transaction.



II. HOW ESCROWS WORK

A. Escrow Rules

- Purchase agreement establishes escrow instructions, which can only then be changed by written agreement of both parties
- Time frames commence from acceptance date; date on which contract becomes binding
- Complete when:
 - all conditions of the escrow have been met
 - all conditions of the parties have been met
 - the parties have received an accounting of the procedure

Terminating an Escrow

- Complete Escrow
- Mutual Agreement
- Court Action – “Interpleader”
 - occurs when there is a disagreement between buyer and seller
 - escrow officer is not a ‘mediator’ but can try to arrive at a resolution
 - escrow officer may disburse funds as a result of:
 - judgment in court action
 - agreement between parties
 - decision of binding arbitration

B. Selection of escrow company

- Is negotiated between buyer and seller
 - either party may choose the escrow company
 - if escrow company is named in listing agreement, cannot be changed without consent of seller or their agent
 - if buyer wishes a different company, salespersons should try to arrive at mutual agreement – must occur before an offer and acceptance occurs
- Licensees prohibited from receiving any “kickback” for placing of escrow business

C. Escrow Instructions

- Formal instructions which are drawn from the information contained in the original agreement (usually signed purchase agreement) as told to the escrow officer
- When drawn and signed, become enforceable, binding contract
- As supplement to original contract, interpreted together
 - conflict between the two, instructions prevail
 - therefore, they should be read carefully

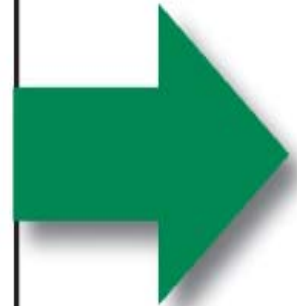
D. Financing Escrow

- Payoff Demand Statement – a formal demand statement from the lender that details the amounts owed to satisfy existing financing in full, as calculated by lender
- Beneficiary's (Lender's) Statement – a demand statement by a lender, under a deed of trust, that provides information such as unpaid balance, monthly payment, interest rates, etc.

E. An escrow example

An Escrow Example

BUYER	John Buyer and Jane Buyer	
SELLER	John Seller and Jane Seller	
SALES PRICE.....		\$800,000
1ST TRUST DEED.....		\$640,000
2ND TRUST DEED.....		\$80,000
DOWN PAYMENT.....		\$80,000
BROKER	J.Q. Smart.....	\$48,000
EXISTING LIENS		
1) 1ST TRUST DEED.....		\$290,000
2) STREET ASSESSMENT BOND.....		\$1,300
CLTA TITLE POLICY PAID BY SELLER.....		\$2,165
Date of Closing is June 1, 2020		



Escrow Example

- Buyer and Seller closing statements usually have different totals, but debits and credits must balance within the statements themselves
 - for buyer, purchase price is a debit
 - for seller, purchase price is a credit
 - for buyer, new loan amount is a credit
 - for seller, payoff of existing loan is a debit

F. Closing Date

- Is the date of recordation of documents
 - Deed
 - Trust deed (if there is a loan, for which property is collateral)
- Closing is the process of signing, transfer of documents, distribution of funds, and reconciliation of buyer and seller accounts



III. PRORATION

Proration

- The process of proportionately dividing expenses or income to the precise date that escrow closes, or any other date previously agreed upon.
- Escrow reports real estate transactions to the I.R.S. using the seller's social security number

30-day base month is used to prorate:

- Property taxes
- Fire insurance
- Interest on loans
- Rents

Proration Example

- Prorate “to” not “through” close date
- If close date the 10th of the month and rent is \$2,000:
 - 9/30 of rent to seller
 - \$600
 - 21/20 of rent to buyer
 - \$1,400
- Property taxes prorated based on seller’s current tax rate
 - Usually 7/1 or 1/1 are the dates from which taxes are prorated



IV. TERMITES AND OTHER PROBLEMS

A. Structural Pest Control Certification Report

- Written by a licensed pest control company and stating the condition and correction cost of any termite, dry rot and fungus damage (called “Section I”) in accessible areas of a structure
 - May be a condition of the escrow
 - FHA and VA loan applications require a pest control report
 - Local custom usually decides who pays, and financial institutions or agencies will decide which one of the parties pays
- “Section II” items are those that if left unattended, may cause structural damage

B. Broker maintains pest control documents

- The Civil Code requires that the broker shall deliver a copy of the Structural Pest Control Certification Report and Notice of Work Completed to the buyer if such report is a condition of the deposit receipt
- www.pestboard.ca.gov
- California Structural Pest Control Board



V. FIRE INSURANCE

A. Fire/Hazard Insurance

- Protects the insured against financial loss due to a fire and other perils on the property
- Necessary, inexpensive compared to the losses due to fire
- All lending institutions require coverage up to the amount of their loan
- Should cover full replacement value of the structure (not necessary to insure the land)
- Extended Coverage Endorsement - insures against all of items on the next two pages

California Standard Form Fire Insurance Policy

- Insures the dwelling against only:
 - fire
 - lightning

Extended Coverage Endorsement will cover:

1. windstorm
 2. explosion
 3. hail
 4. aircraft
 5. smoke
 6. riot
 7. causes not attributed to a strike or civil commotion
- Earthquake coverage is totally separate coverage

B. Fire Insurance Proration

- When purchasing property, a buyer usually obtains a new policy
- Agent for buyer should determine if property is 'rated' by insurance company due to prior claims on property
- Fire insurance is often part of a homeowner's insurance policy and is prorated in Escrow

C. Coinsurance

- A clause in a policy that requires the property owner to obtain a separate policy, usually to insure 80% of the value of the dwelling or receive only a percentage of reimbursement for fire loss

C. Coinsurance (cont'd)

VA 48

HOW NONRESIDENTIAL COINSURANCE WORKS

HOW NONRESIDENTIAL COINSURANCE WORKS

1. Actual value of your improvements	=	\$200,000
2. 80% coinsurance clause requires you to carry fire insurance on 80% of the actual value of the dwelling. (80% of \$200,000)	=	\$160,000
3. Amount of fire insurance carried (Face amount on your policy)	=	\$120,000
4. Ratio of loss payment \$120,000 (actual amount) \$160,000 (required amount)	=	75%
5. If your actual fire loss is	=	\$80,000
6. Your insurance would pay 75% of actual loss (75% of \$80,000)	=	\$60,000
7. Your out-of-pocket cost would be the loss less insurance payments (\$80,000 - \$60,000)	=	\$20,000



VI. TITLE INSURANCE

Title Insurance

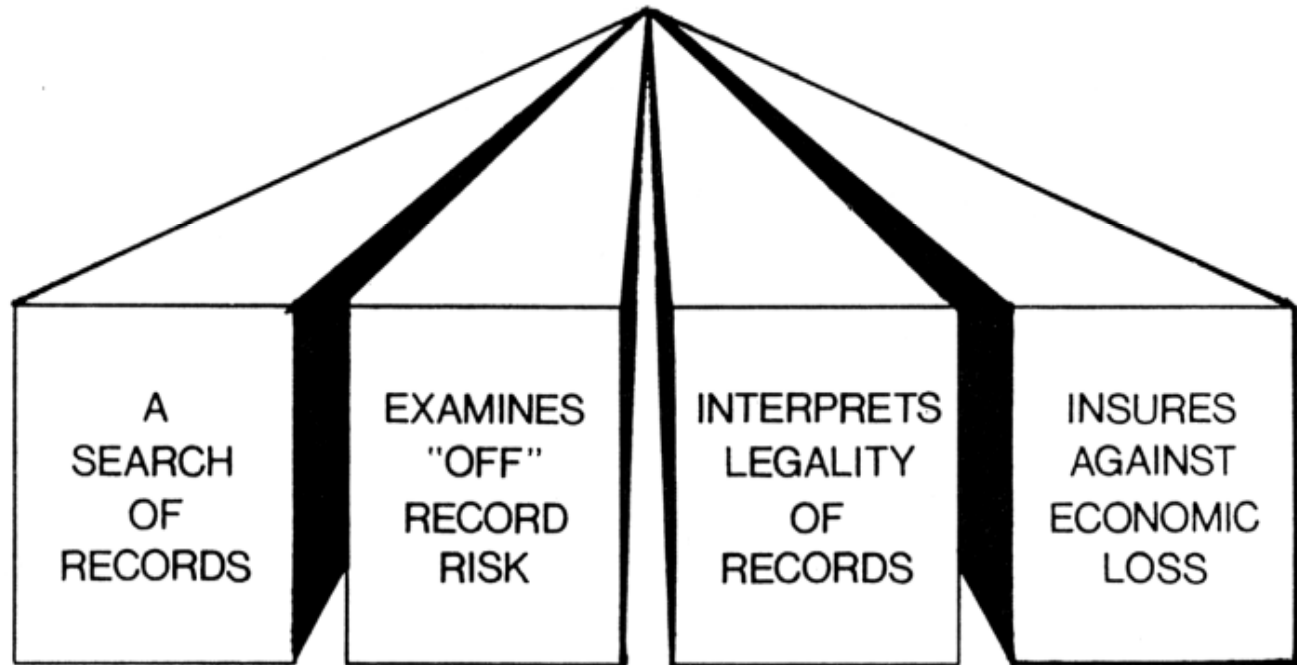
- Insurance designed to protect property owners and financial institutions against losses which result from imperfections in title

A. Chain of Title

- A recorded ownership history of a specific property (from the 'beginning of the earth' until the date on which the report is issued)
- Title Plant - the compiled information on the chain of title of a specific property gathered by title insurance companies and stored in computers

B. 4 Functions of Title Insurance

TITLE INSURANCE FUNCTIONS



C. Preliminary Title Report

- A report showing the condition of title before a sale or loan or transaction, includes:
 - name of owner and description of the property
 - list of any outstanding taxes, bonds, or other assessments
 - any CCRs (covenants, conditions, restrictions)
 - any recorded liens or other encumbrances
 - loans
 - easements

VII. TYPES OF TITLE INSURANCE POLICIES

A. CLTA

- California Land Title Association Standard Coverage Policy Form
- CTLA is the acronym for the state trade association
 - insures against all items of record
 - most often used

CTLA also insures against “off-record” risks such as:

- a. forgeries
- b. acts of minors and incompetents
- c. acts of an agent whose authority has terminated
- d. invalid deed delivery
- e. unrecorded federal estate tax liens
- f. undisclosed rights of husband and wife
- g. expenses incurred in defending title

CTLA does NOT insure against:

- easements and liens which are not shown by the public record – this requires an ALTA policy
- rights or claims of persons in physical possession of the land (ALTA yes)
- unrecorded claims not in public record that could be ascertained by physical inspection or correct survey of the property (ALTA yes)
- mining claims, reservations in patents, water rights and government actions such as zoning ordinances (ALTA yes)
- www.clta.org / California Land Title Ass'n.

B. American Land Title Association Policy (ALTA)

- Insures against all CLTA risks
- Extended coverage includes many of the exclusions to the CLTA policy as shown in previous slide
 - still there are exceptions to ALTA Policy
- Generally required by California lenders and by out-of-state lenders unable to make a personal inspection of the property – this policy does require an on-site inspection

Exceptions to ALTA coverage

- ALTA Policy does not cover:
 - a. defects known by the insured at the time the policy was issued but not designated in writing
 - b. government regulations concerning occupancy and use such as zoning

- www.alta.org / American Land Title Ass'n.

C. **ALTA-R Policy**

- Is recommended by title companies for one-to-four unit owner-occupied residential dwellings
 - does not include a survey because property boundaries are established by subdivision map

D. Who Pays Title Insurance Fees

- Customarily paid by:
 - the buyer in Northern California.
 - the seller in Southern California.



**VIII. REAL ESTATE
SETTLEMENT
PROCEDURES ACT
(RESPA)**

RESPA

- Required forms and specific procedures involving 1-4 unit residential units
- States that the precise closing cost of a real estate transaction must be made known to the borrower at least one business day before escrow closes
- Allows borrowers to shop for settlement services
 - Lenders must provide a booklet entitled “Settlement Costs and You” within three business days of receiving a loan application
- Enforced by HUD

Other provisions rule that:

- The lender must provide a good faith estimate of the total closing cost to the borrower at the time of the loan application or within three business days along with information booklet
- The escrow company must furnish a uniform settlement statement to the borrower often called the HUD-1

Other provisions rule that:

- Escrow and title insurance companies are prohibited from giving or receiving kickbacks
 - this excludes co-op broker fees and referral agreements between brokers
- No seller may require a buyer to purchase title insurance from any particular company as a condition of sale



**IX. CALIFORNIA ESCROW
ASSOCIATION**

The California Escrow Association

- Has developed a statewide program to promote professional service and educational opportunities for its members
- Several community colleges have established certificate courses for escrow personnel and real estate brokers
- www.ceaescrow.org (California Escrow Association)

HOMework

- Read Chapter 8
- Study for quiz
- Continue reading your supplemental text and be prepared to give oral book report

Chapter 7 Summary

- Escrow created with
 - Deposit receipt
- Valid Escrows need:
 1. Signed instructions
 2. Neutral party
 3. Conditional delivery
- Escrow complete:
 1. All conditions met
 2. Parties receive accounting
- Payoff demand
- Beneficiary's statement
- Closing date
- Can be terminated by:
 - Completion
 - Mutual agreement
 - Interpleader

Chapter 7 Summary (cont'd)

- Proration
 - Property taxes
 - Fire insurance
 - Interest
 - Rents
- Structural Pest Control Report
- Chain of Title
 - Title plant
 - Preliminary title report
- CLTA
- ALTA
- ALTA-R
- RESPA