

Special Report

Avoiding & Resolving the Eight Most Common Probate Realty Problem Areas

- *What to avoid when considering new cases*
- *How to identify “red flag” warning signs*
- *Remedial actions and how to best implement*
- *Checklist items to incorporate with initial client contact*

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Avoiding & Resolving the Eight Most Common Probate Realty Problem Areas

By Rick Harmon – The Suburban Group

The purpose of this report is to: 1) help the probate practitioner identify potential pitfalls before accepting cases; and 2) provide solutions to problems discovered during the course of administering estates and trusts.

How many times have you represented a client's probate or trust that you wish you'd never have taken the case because of real estate related problems? Many of the problems that I encounter relating to estate realty (usually during the course of making a loan) could have been avoided. While some are unavoidable, many could be eliminated or minimized by proper planning prior to, or upon opening, probate.

I've written this report with the intent of simplifying the topic areas, keying in on many of the most frequently encountered problems and identifying ***red flag*** areas. You will have undoubtedly experienced other problems not discussed on these pages. Most practitioners could fill volumes of textbooks that cover what can and does go wrong with estate property.

It's my personal objective that the reader further develops his/her intuitive senses for potential pitfalls, anticipating the scenarios that may arise from problem files and recognizing the need for involving other experts early in the process.

If there was one single suggestion I'd make to an attorney beginning probate practice, it's: ***"Begin with the end in mind."*** Know the answer to: "How will the estate pay creditors or other bills? How will you get paid? Is the client prepared to liquidate the estate or finance debts to facilitate the close of probate?" Asking probing questions and gaining agreement as to a plan will go a long way to a smoother probate.

Your own checklist should include questions relating to these key problem areas:

1. Equity
2. Title Insurability
3. Financial condition
4. Habitability
5. Building Insurability
6. Security
7. Availability
8. Marketability

This report will briefly discuss each of these eight problem areas so that you may develop your own sense of what matters most to you. At the end I've included a list of Do's & Don'ts that you may incorporate as part of your own initial client interview questionnaire.

Equity:

The big red flag! If I were to choose one major error that attorneys make that neither I nor anyone else could fix, it's the probate case consisting of a property with very little equity. Anything less than 20% equity will not be sufficient to pay costs of liquidation, attorney's and personal rep's statutory fees. Resolving a messy probate concerning a property with 50% equity will generally have many more options available.

To avoid: Your prospective client may not be entirely forthright (imagine that!) as to the true status of the decedent's realty. My experience is that a factual misrepresentation by a prospective client will often lead to a less-than-cooperative client as the real facts unfold. Ask yourself, "Does this property's equity merit your representing this client and your getting paid?" Are you prepared to work *pro bono* should there be insufficient equity to pay secured lenders and the cost of sale?

Available Solution(s): Preferably, avoid at all cost. You can fix a lot of problems, but typically, not this one. Ask lots of questions during initial client interview before taking on such a case. Determine equity by independently checking property values and encumbrances for subject property, remaining especially sensitive to issues such as property condition, cash flow and possession.

A twist to the "this isn't going to work no matter what" is the personal rep. that is also sole heir who might be able to raise your fees out-of-pocket or via credit card, providing that there are only minimal debts. Alternatively, the real property could be distributed to the heir subject to the debt. This is risky, however, as an unanticipated creditor claim could ruin your whole plan.

Title Insurability

Clouds in the chain of title and vesting deficiencies are the second biggest problem realty area. Mortgages made by government agencies that don't require repayment until death or transfer, also called "silent seconds," is a fairly common surprise. Involuntary liens such as defaulted property taxes, bail bonds and judgments are common problems that delay the close of transactions.

To avoid: Red Flag: Don't depend on free title company profiles or last recorded deeds! Provide your title company a *Statement of Information* regarding the decedent, and then obtain a preliminary title report early if there is any chance of a real estate loan or sale transaction occurring. Confirm the vesting to be as you expected and discuss any surprise liens with your client in case they can produce proof of payment sufficient to satisfy the title company.

Available Solution(s): I urge you to develop a direct business relationship with a title company and have a sales representative assigned to your firm. There are perhaps two-dozen title insurance companies in Southern California alone; some are better than others based on financial strength and service. We like Old Republic Title because they listened to us many years ago when the other big companies wouldn't. They still listen today and also make their top-level legal staff accessible to my attorney clients and myself.

Call Larry Christian, Old Republic Title Company at (800) 388-4853 X6509.

Financial condition:

Are all secured creditors (i.e., mortgage lenders) payments current? Is client aware of any outstanding liens or other claims that will surface during the administration of probate?

To avoid: Get copies of all secured lenders documents and payment histories. Write to secured lenders via certified mail (you may expedite their response by providing a copy of death certificate and your client's Court Letters. Determine account status, balance, and clarify with client who will be making the payments. **Red Flag:** Watch for procrastination behavior by the client as to their P/R duties.

Available Solution(s): Correct delinquent or defaulted loan arrearages immediately. Exhaust estate resources first, as this will minimize commingling of estate and personal assets. Consider quick-selling personal property belonging to the estate to raise cash, auctioning real estate or having the personal rep. obtain an equity-based mortgage. If borrowing, consider obtaining sufficient funds to pay future loan installments, taxes, insurance, maintenance expenses and repairs.

Red Flag: *Don't expect foreclosing lenders to notice you or your client automatically just because you made a phone call. Noticing by foreclosure trustee to persons others than the Trustor (deceased borrower) or junior lien holder is generally regarded as voluntary.*

Also, don't forget to file a Preliminary Change of Ownership (PCOR) with the County Recorder on a timely basis. Be prepared to clarify all Prop 13, Prop 58, Prop 103, escaped and supplemental tax issues with your client (this can be very time consuming).

Habitability:

Habitability relates to issues surrounding security, safety and health. These generally result from deferred maintenance or structural damage but could also relate to a leaking roof, debris in or around premises (including "pack rat" habits), exposed electrical or plumbing, open holes or access points on or in subject property [**Red flags**]. Also, building code violations, incomplete construction work or damage to building can cause a loss of a Certificate of Occupancy.

To avoid: Ask the client "what is the condition of the property and the surrounding premises?" If uncertain as to the true condition, ask for photos of subject property, discuss with the probate referee (if a physical inspection was made...some still do!) or obtain a Form #2055 appraisal from a California State licensed real estate appraiser and ask for interior photos. If all else fails, visit the property yourself, wearing the appropriate protective clothing and a "be-prepared-for-anything" attitude.

Available Solution(s): Fix it, clean it, remove it or plug it. These types of problems generate lawsuits and energy-wasting disputes between estate rep's (as landlords), tenants, neighbors and passer-by's. You or your client may be fortunate enough to know a reliable handyman or contractor

qualified to resolve the problem(s). We have assembled a small list of licensed contractors that may be able to help. Another viable plan is to contract with a Dept. of Real Estate licensed property management company and employ them to resolve any and all habitability problems, including local (City) government concerns.

Building Fire/Hazard Insurability:

As hard as it is to believe, at least 75% of the estates that we see having free and clear property have no insurance whatsoever. Putting the liability issue aside momentarily, this is a recipe inviting disaster. Oddly, attorneys seldom bring this to my attention before we discover this fact while processing probate loans. Estate assets and fiduciaries are at risk with tenants, neighbors, civil servants and even other heirs who visit the subject property. If the property is vacant, the empty building can be a magnet to transients and vandals.

To avoid: Obtain a copy of your client's evidence of insurance (called a declaration page in the industry). Review the policy to confirm that it is current, coverage, limits and note when the next payment is due. Also consider counseling your client as to obtaining an umbrella insurance policy if they have substantial personal (non-estate) assets at risk.

Available Solution(s): Make certain that your client has a current policy for the estate realty in effect now. Obtain a tenant policy if anyone other than a sole heir/personal rep. occupies the estate property. If your estate consists of substandard realty, consider F.A.I.R. plan insurance underwritten by the State of California. Not all insurance agencies offer this product, as I understand it is not very profitable to agents. If the subject property is vacant it will be even more difficult to obtain coverage since this is a high-risk property. I recommend developing a strong business relationship with an insurance agency that is well versed in this type of situation.

Need an insurance agency that understands the needs of probate estates and trusts? We use **R. M. Sorenson & Associates at (800) 341-4860**. Ask for Mr. Dick Sorenson.

Security:

Security relates to the factors that affect the ability for the subject property to qualify for new financing. An easier way to think of this is, were the unthinkable to occur and the property reverts back to the lender by foreclosure, how marketable is the property for a lender? This topic relates with the marketing factors discussed later in this report.

To avoid: Ask clients a few probing questions about the condition of the subject property. **Red flag:** Determine if there is anything unusual about the property type, condition, design or location that would limit the appeal of retail buyers. If deferred maintenance is present (typically there is *some*) ask your client if it appears substantial (leaky roof, visible termite damage, structural cracks, foundation problems or soil erosion).

Available Solution(s):

My assumption here is that the estate desires to know the true condition of the subject property. However, if selling, the personal representative must disclose all known property defects, even if

selling “as is.” A prudent seller of estate property would want to disclose any possible defects and require the buyer to perform his or her own due diligence.

A licensed appraiser may be the first step in identifying potential problems. An appraiser may deduct value for out-of-date décor, such as flocked wallpaper, but will flag suspicious-looking ceiling stains (leaky roof?) or cracks (earthquake damage?). Using a home property inspector will be more thorough in identifying problem areas. Also, civil or structural engineer may be consulted to address concerns with structural cracks and soil concerns.

Availability:

This topic relates to property possession issues. When heirs, relatives and acquaintances occupy estate property, most disputes arise from issues related to obtaining market rents from property. It’s not unusual for these persons to believe they have some sort of entitlement if they’ve lived in the property for free for an extended period and it’s not uncommon for me to see several heirs or “shirt-tail relatives” squatting in estate property.

Evicting known persons can be a delicate and frustrating experience for most executors and administrators because of their familiarity of the parties and reluctance to take a strong position on the matter. Meanwhile, the property sits idle as an unmarketable estate asset.

To avoid: I’d strongly recommend obtaining a written rental agreement specifying the terms and conditions under which the tenant (including an heir) may continue to occupy subject property. All persons known to occupy the premises should be acknowledged. Also, professional property management ought to be used for P/R’s who have neither the time nor temperament to deal with the business of renting property to others.

Available Solution(s): Familiarize yourself and your client with the timeline issues relating to unlawful detainers. Consider offering money to tenant if they’ll leave, but not until they’ve vacated. This is the easier, softer solution if you can make it work. Need a law firm specializing in evictions? Contact ***Ms. Layne Liddle, at Liddle & Liddle***, in Glendora. She can be reached at ***(626) 963-1638***. She has assisted several of our clients and has been professional, courteous, cost-effective and stayed on top of her files in a timely manner.

Marketability:

This typically relates to the ease of attracting a qualified buyer. The ideal property is a single-family home in a desirable location, in excellent condition and move-in ready.

To avoid: Many estates contain realty that is defective, non-conforming, or unusual. Does a large market exist for your client’s estate realty in its current condition? Will this property appeal to retail buyers or investors? Is it located in a desirable community? Does this property have *curb appeal*?

Red flag: Is conventional mortgage financing readily available or will seller purchase financing be necessary? Is there a market for your desert land, gas station, mixed-used commercial property or geodesic dome house? (I’ve seen them all!)

Available Solution(s):

When selling probate real estate, the first priority must be to determine the market the property will be targeted towards. Your real estate professional ought to know something of the demographics and financial profile of prospective buyers for your property. If the subject property is located in an area where low-down, FHA financing is the norm, make certain that the property (not just the buyer) will qualify for FHA financing. Some properties will not qualify for any outside financing, so expect to either carry back “purchase money” or be prepared to discount the price sufficiently to attract a cash buyer.

We work with many clients who borrow to renovate estate property in order to attract a retail buyer. What can you do to maximize the appeal of the subject property without overspending? It’s not unusual for an estate to borrow \$15,000 to \$30,000 with the objective of fixing up a property and doubling the money (or doing better). Such a high return on investment will often reduce the time to sell when property is clean and attractive.

Do’s & Don’ts:

1. **Do** have an exit plan. How will the P/R be paying your bill; by borrowing, selling or cash on hand? **Don’t** count on estate’s liquidity improving at the end of probate.
2. **Do** watch out for estate property with tight equity. Few options, if any, exist to correct for insufficient equity. **Don’t** take the client’s word; **do** independently determine how much equity really exists.
3. **Do** develop your own dependable source(s) for sales comps and appraisals.
4. **Do** develop input forms and checklists for new clients to screen for potential pitfalls
5. **Don’t** count on title company property profiles to determine condition of title.
6. **Do** obtain a preliminary title report if client will be selling or borrowing within one year of obtaining. We frequently see trusts that were not properly funded or have other avoidable pre-existing title problems and transfers of title-clouded property.
7. **Do** write to lenders. **Do** use certified mail. **Don’t** depend on a telephone call. Lenders **do** foreclose on estate realty without noticing P/R’s or attorneys. Really **do!**
8. **Do** know who will be paying the mortgage(s), taxes, insurance and maintenance. The “little red hen syndrome” is common among multiple heirs.
9. **Do** determine who occupies the property (if anyone). **Do** ask for a list of all persons known to be living in the property. **Do** inquire who is paying rent and/or expenses.
10. **Do** consider requiring relatives and casual tenants to sign a rental agreement to establish rent value and date to vacate.
11. **Do** inquire as to the condition of the property. What repairs are needed? Any health and safety issues? Are the premises kept clear of debris? Any other problems?
12. **Don’t** be surprised when the deferred maintenance interferes with the subsequent sale or buyer’s financing of property.
13. **Do** make certain property is currently insured. **Do** get policy info and demand current declaration page to assure that coverage is in effect and has not lapsed.
14. **Do** consult with your outside experts as early in the probate process as possible.

Conclusions:

1. Begin with the end in mind. Have an exit plan.
2. Ask probing questions up front to avoid surprises
3. Verify facts for yourself (clients are great “spin doctors”)

4. Use your experts and resources early and frequently

More Resources:

www.closeprobate.com has an entire section devoted to legal professionals and your needs for forms, checklists, worksheets and links to other sites providing services, expertise and information. You can even add your name to our legal professional directory.

Call or email me at Rharmon@closeprobate.com. I'm always available to discuss your probate or trust real estate matter.

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