

Speaker Lisa Pertersen's Bio

Lisa A. Petersen is Underwriting Counsel and Back Up State Counsel for the Fidelity National Title Group, which includes Chicago Title Insurance Company, Fidelity National Title Insurance Company, and Commonwealth Land Title Company. Her responsibilities include statewide underwriting for all companies. She enjoys the education component of her position. She has created several educational tools for the agency network, including Friday FAQs, Title Tuesdays and Lunch & Learns. Lisa has also created numerous seminars for our agents and their customers with Title 101 being the most popular. Lisa creates the annual Webinar schedule with topics based on agent suggestions. She loves the opportunity to travel across the state to meet with our agents and present seminars to their staff members, as well as their customers. Lisa is a member of the State Bar of Wisconsin and the Milwaukee Bar Association where she serves as a speaker on various title insurance topics. She served on the Board of Directors for the Wisconsin Mortgage Banker's Association and was a member of the Wisconsin Commercial Real Estate Women. She is also a member of the American Land Title Association and the Wisconsin Land Title Association where she is an active member of the Education and Legislative Committees. Lisa is a Past President of the Wisconsin Land Title Association and served on its Board of Directors for 7 years. She received her BA from the University of Wisconsin-Madison and her JD from Northern Illinois University and is a frequent lecturer on title issues across the state.

Wisconsin Land Title Association (WLTA) Activities

Appointed member of WLTA Commissioner of Insurance Task Force

WLTA Past President

WLTA Education Committee Chair

WLTA Legislative Committee Member

Recipient of many WLTA awards including the President's Award, Committee Chair of the Year, Committee Member of the Year, Service Award, Golden Key Award, Michael F. Wille Leadership Award

WLTA Instructor (Certificate Courses/Pre Licensing) 1999-present

Fidelity National Title Group Awards

Ticor Title Service Award

Chicago Title Insurance Company Circle of Excellence Award

CLOSING ERRORS YOU CAN AVOID

Statements and Representations by Closers

- Closer is not an attorney for the parties
- Closer has a duty to speak truthfully
- Closer is liable if he/she vouches for someone or something
- Closer is a neutral party who cannot take sides

Duties Regarding Handling of Funds

- Duty of reasonable care in handling funds
- Adhere to the Good Funds Law-no exceptions!
- If money belongs to several people, obtain joint instruction
- Duty to invest? Make your position clear
- Duty of reasonable care in disbursing funds
 - Agent of lender at a loan closing
 - Do not let seller's pay off their own liens

Duties Regarding Recording of Documents

- Record all documents immediately.
- Record in the proper order.
- Keep a log of the documents whereabouts.
- Review document for completeness.
- Lost documents, what to do? Lost Instrument Affidavit is only a temporary fix.
- Affidavits of Correction

Mortgage Payoffs

- Must be in writing and should reference loan number and property address in addition to borrower's name
- Watch home equity lines of credit!
- Put sufficient detail on the payoff check.
- If property is in foreclosure, make certain you have accounted for any attorney's fees.
- Do not let the Seller deliver their own pay off check.

Short Sales

- Short sales can occur when a seller can't afford to make their payments and is nearing foreclosure or bankruptcy.
- Most short sales occur when the seller owes more on their house than they can sell it for. They are often referred to as being "upside down".
- The causes can range from changes in interest rates (ARM's), to personal finance issues to loss of employment to divorce, family illness or death.

What is a “short sale”?

A short sale is an “arrangement” between the homeowner and the lender wherein the lender agrees to accept less than the amount of outstanding debt in satisfaction of their mortgage. The lender is agreeing to get “shorted”.

There are three basic stages of a short sale:

1. Determine what is owed on the property
 - Order a preliminary title commitment
 - Review judgments, liens, taxes
 - Have an estimated closing statement prepared
2. Determine the estimated sales price
 - Review comparables and pending/active listings in the MLS
 - Remember that the Lender will likely insist upon an appraisal prepared by a reputable appraiser (perhaps at their choosing)
3. Determine whether or not there will be sufficient funds to pay off all of the existing liens based on the preliminary numbers you have compiled
 - Review outstanding judgments, liens and taxes as shown on the preliminary, estimated closing statement vs. the anticipate sale price using comparables and MLS listings

If it appears that there will be insufficient proceeds to cover the outstanding monetary items, the seller may request a short payoff from the lender.

Why would a lender agree to accept less than they are owed in a sale transaction?

- To avoid the cost of foreclosure (lenders lose on average, \$50,000 per foreclosed home)
- To avoid adding to their REO inventory (REO=Real Estate Owned)
- Seller has a true hardship and is a likely candidate for filing bankruptcy
- Property values are depreciating
- Property is in poor condition (fire, flood)

What will the Lender require? Lender requirements will differ, but most will require at least the following:

- Copy of the signed Offer to Purchase
- An estimated closing statement
- Title commitment
- Hardship letter from the seller
- Appraisal or solid market analysis
- Current financial information on Seller
- Copy of Buyer’s loan application

What is the role of the Seller?

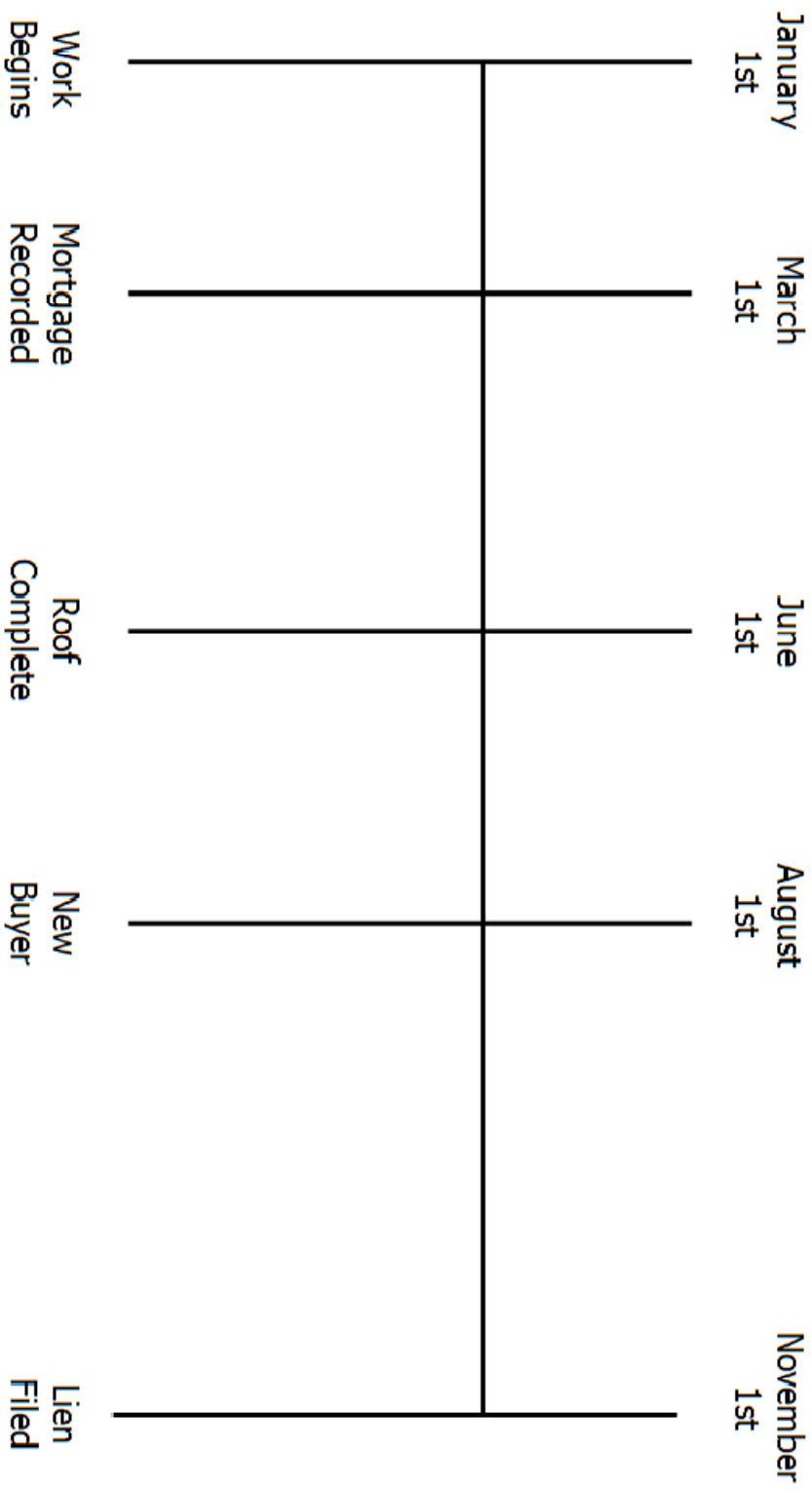
- The Seller should contact the Loss Mitigation Department for the lender to make sure they will even consider a short sale and what the requirements for sale will be.
- Many lenders have a short sale packet.
- Inform all potential buyers that this will be a short sale and that the lender's written approval will be required. Include language in the Offer to Purchase.
- Understand that it can take 45-90 days for a lender to approve a short sale.
- The lender may also require the seller to sign an unsecured note for all or a portion of the deficiency.

What is the role of the closer?

- **FOLLOW THE LENDER'S CLOSING INSTRUCTIONS TO THE LETTER.**
- You must pay very close attention to all of the lender's written instructions. If there is even the slightest change in the closing statement/HUD, you must get written approval from the lender.
- Provide the lender with all requested documentation well in advance of closing so that you are able to obtain written approval to close.
- Remember that there may be other lien holders that will also be shorted or not paid at all, and they must also consent in writing.
- You must have a commitment in writing from each and every lien holder that they will issue a satisfaction or a release at or immediately following closing—**especially** those that are not going to receive payment, they still must commit to satisfy or release their liens. Possible exception: Judgment creditors on homestead property.
- Lender's instructions will specify what monetary items will be paid at closing, typically realtor commissions (lender may impose a cap), taxes, title fees and attorney's fees.
- Most lenders will not allow credits for closing costs or repairs.
- Verify that the lender's payoff includes any applicable attorney's fees.
- **HAVE SOMEONE VERIFY YOUR WORK.** In most cases, the lender is relying on your estimated HUD (at least in part) when agreeing to accept less than the amount it is owed.
- Update the commitment immediately prior to closing. If a bankruptcy court sits in your county, you must conduct a bankruptcy search.

In today's market, you may begin to see more closings that are based on "short sales". You **MUST** use extra care when closing a short sale. This is an area ripe for fraud. Use your best instinct—if it doesn't feel right, smell right or look right, **DO NOT CLOSE IT.**

CONSTRUCTION TIMELINE



CONSTRUCTION DISBURSEMENTS

Introduction

Once a property owner and a lender agree to the terms of a financing package for the construction of an improvement on the owner's land, a procedure must be set up for the proper disbursement of the loan funds to the parties that actually provide the labor and materials to construct the improvement. The reason for this, from the lender's perspective, is twofold. First the lender wants the improvement to be completed so that if the loan is foreclosed the security for the loan – the improvement – will have a set value at least equal to the amount of the loan. Secondly, the lender generally does not just give the loan funds to the borrower and allow the borrower to pay the contractors. Rather, the lender retains control of the loan funds until the contractor's draw requests are paid. The Wisconsin Court of Appeals has ruled in *First National Bank vs. Wernhart* {204 Wis. 2nd 361, Ct. App. 1996}

'... that a mortgage lender who consents to disburse the loan proceeds and personal funds of the borrower, without further participation by the borrower, is an agent of the borrower and therefore owes a duty of due care to assure the funds are paid for work actually done and to assure that the contractor has obtained lien waivers from subcontractors.'

If the lender breaches that duty of care it will be liable for losses incurred by the borrower which are attributable to that breach of duty. Fulfilling that duty of due care can be a time consuming and rather complicated task. Rather than incurring the expense of training their own employees to properly monitor the disbursement of construction loan funds, lenders frequently turn to title companies to perform the disbursing function.

In addition to the lender the following parties, who oftentimes have differing interests, will be involved in the construction loan disbursing procedure.

The owner wants the improvement to be completed in the shortest period of time for the least amount of money and he only wants to pay for the improvement once. The owner, generally, also wants the improvement to be a "Cadillac" even if he is only paying for a "Chevrolet".

The person or entity that agrees with the owner to construct the improvement is the contractor, sometimes called the general or prime contractor. The general contractor (hereafter called "general") wants the improvement to be completed as soon as possible so that he can move on to other projects. He wants to be paid immediately as the work progresses, and sometimes even before the work is completed. He does not want to submit much in the way of "paperwork" before being paid and he wants to wring as much profit out of the project as he can. Therefore, while the owner might think that the contract price might befit a "Cadillac", the general would like to provide the improvement for the price of a "Chevrolet".

While the general will perform some of the work to construct the improvement, he will not do it all. He will hire other contractors to perform work that he either cannot perform or does not wish to perform. He will "sub-contract" some of the work called for in his contract with the owner to a subcontractor (hereafter called the "sub"). The

relationship between the general and the sub is similar to the relationship between the owner and the general. The general wants the sub's work to be high quality; be performed quickly; and be done at the lowest cost to the general. The sub wants to be paid immediately (or sooner); does not want to be bothered by paperwork; and wants to wring as much profit as he can out of the project.

The general and the sub can only perform their work if they have construction materials or supplies to work with. The material suppliers from whom they obtain their supplies expect to be paid for the materials as soon as the general or subs are paid for their work.

Finally, the owner and lender would like some safeguard to be sure that construction loan funds are distributed to those who have performed work on or provided materials for the construction of the improvement. In most cases, however, the escrowee is instructed to make one payment per draw to the general contractor. Thus, the ultimate duty to pay the subcontractors rests on the general contractor and the disbursing agreement does not assure payment to the subcontractors. The escrowee, therefore, is typically instructed to collect the documents necessary to defend against any lien claims if the general contractor fails to pay subs and suppliers.

Beginning a New Construction Disbursing Project

When you begin a construction project, you will review two essential documents: the Disbursing Agreement and the Contractor's Cost Breakdown. You will prepare a spreadsheet for the project based on the cost breakdown. You are encouraged to use the Construction Project Checklist attached to these materials as you begin a new project.

I. Disbursing Agreement

The disbursing agreement is the instruction from the owner and lender to the escrowee as to the disbursement of funds and collection of evidence that parties have waived their lien rights. The escrowee should review the loan agreement and building contract, if it has those documents, to verify that they are consistent with the disbursing agreement. **The escrowee should not disburse any funds unless the disbursing agreement has been executed by the owner and lender.**

The agreement should, at a minimum, address the following:

- The party(ies) to be paid by the escrowee
- Whether waivers are to be current or on a draw delay
- Responsibility for periodic inspections of the work
- What the escrowee does if a lien is filed
- Limitations of the escrowee's liability
- Termination of the agreement and resignation of the escrowee
- Fees for the services of the escrowee

Parties to be paid by Escrowee. The owner and lender sometimes instruct the escrowee to make payments directly to all subs and suppliers listed on the draw requests. The goal of direct payment is to assure that subs are paid, in addition to having waived their lien rights. The agreement often calls for the escrowee to exchange a check for a proper waiver.

Direct payment often conflicts with the building contract, which requires that all payments be made to the general. Before agreeing to a direct-payment plan, the escrowee should verify that the general contractor is in agreement with the plan.

Waivers Current or on Draw Delay. On the other end of the spectrum from direct payment is receipt of waivers one draw after payment is made for each line item. Frequently, the general will claim that he is in a “Catch 22” situation regarding the waivers – he cannot obtain the proper waivers unless he pays the subs/suppliers, but he cannot obtain the funds from the escrowee unless he presents the waivers. The general will then request permission to submit the waivers on what is called a “draw delay basis”. In that situation, the general submits his waiver for the entire amount of the draw. The escrowee pays the entire amount of the draw to the general on the condition that before the escrowee releases the next draw to the general, the general must submit all the lien waivers for the current draw to the escrowee. Obviously, the draw delay submission of waivers is available on interim draws only. The final draw request can never be released until final lien waivers have been received from all the proper parties.

Before agreeing to accept waivers on a draw delay basis, the escrowee must obtain a written amendment to the disbursing agreement signed by the owner and the lender, which clearly instructs the escrowee to collect waivers on a draw delay.

The escrowee must consider whether or not it is able, in its other role as policy-issuing agent, to produce policies giving the requested construction lien coverage if the project is on a draw delay. When the lender has statutory priority over construction liens, the Company will provide the lender with pending disbursement construction lien coverage even if the project is on a draw delay. However, if the lender does not have statutory priority, or the owner has or will receive any protection against construction liens, you must call Company counsel to obtain approval to sign a disbursing agreement providing for draw delay. Our **minimum** requirements to give such coverage are:

An acceptable current financial statement from the general contractor, and

An indemnification agreement from the general holding the underwriter harmless from all construction lien claims.

Inspections. The escrowee may elect to inspect the project on behalf of the lender in order to assure the lender that the work which the general completed is, in fact, completed. The escrowee should not, however, assume the owner’s responsibility to monitor the workmanship on the owner’s own project. The owner must inspect the project himself or hire an inspecting architect to do so on the owner’s behalf.

Escrowee's Duties When a Lien is Filed. The agreement should explain what the escrowee's duty is when it discovers a filed lien. Normally, the agreement requires the escrowee to search title with each draw. If a filed lien is discovered, a reasonable requirement is that the escrowee notify the owner and lender. The agreement should say that the escrowee does nothing further until it receives joint instruction from owner and lender as to how the lien is to be handled. The agreement may specify the ways a lien will be dealt with: bonding off, satisfaction, funds escrowed for payment of the lien.

Limitations on Escrowee's Liability. The disbursing agreement should clearly reflect the fact that the escrowee does not set or control the design, construction schedule or cost of the improvement. The agreement should clearly state that the escrowee does not assure that: (1) the project will be completed; (2) that if completed it will be in accordance with the plans and specifications; or (3) that there are sufficient funds available to complete the improvement.

Termination of the Agreement. The disbursing agreement should permit the escrowee to resign. On occasion, situations may arise with an owner, lender or general which make it impossible for the escrowee to properly perform the duties called for by the disbursing agreement. The escrowee cannot be forced to continue to participate in the project if it cannot comply with the terms of the agreement.

Escrow Fees. A provision for fees must be in the agreement. The fee should be specifically stated in the agreement and it should at least be of sufficient size to cover the escrowee's costs.

Parties to the Agreement. The disbursing agreement is generally entered into by and between only the owner, lender and escrowee. However, it is typically a good practice to have the general contractor consent to (agree to obey) the disbursing agreement. The building contract entered into by the owner and general might have terms that conflict with the terms of the disbursing agreement. For example, the construction contract might not require the submission of lien waivers or it might not require the submission of detailed draw requests. If the general does not consent to the disbursing agreement, which gives the GC the chance to review the disbursing agreement's terms, inconsistencies may not be discovered until the first draw.

II. Contractor's Cost Breakdown

The contractor's cost breakdown is prepared by the general. It is a list of all the categories of work that will be performed by the general and subs. It must disclose the names of all the subcontractors and/or suppliers who have contracted with the general together with the amounts of their respective contracts. The sum total of all the contracts must equal the sum total of the loan funds and the owner's equity (contribution).

The contractor must affirm on the breakdown that the information on the breakdown is correct and that it has disclosed the names of all the subs and suppliers that the general has contracted with. That disclosure is a crucial element in determining the responsibility of the escrowee to insure that funds are disbursed to the proper parties. It also indicates the parties who might have a right to file a lien against the improvement and, therefore, who must supply lien waivers to the escrowee.

Escrowee's Spreadsheet

Use the cost breakdown to prepare your spreadsheet. The spreadsheet is a tool for the escrowee's internal use. It lists all of the line items for the project, just like a cost breakdown, but has additional columns to allow you to post the information received with each draw. The spreadsheet allows you to track the identity of subcontractors and suppliers. It also lets you keep continual track of changes in the contract price, so that if the contract price changes you confirm that there are change orders which match the changes shown and you can confirm that there is enough money to pay for the entire project.

Reviewing a Draw Request

With each draw request, the escrowee will typically receive the following information:

- Contractor's draw request
- Owner's certificate or authorization
- Inspection report
- Survey (first and last draws, typically)
- Waivers
- Completion Affidavit (last draw only)
- Punchlist Escrow (last draw only, as needed)

The escrowee will typically perform the following duties:

- Update title to a current date
- Advise the lender (and owner, if agreement so states) of new title matters
- Review documents received
- Collect 1099 reporting information
- Post draw request information to escrowee's spreadsheet
- Perform inspection, if escrowee is doing the lender's inspections
- Review survey and advise lender of any survey matters shown
- Advise lender that the draw is acceptable
- Receive and disburse lender and owner equity funds
- Issue pending disbursement endorsement to lender
- Enter 1099 reporting information into year-end report schedule

The duties to be performed in a typical draw request are discussed below. You are encouraged to use the Draw Request Checklist attached to these materials with each draw request.

Contractor's Draw Request

The contractor's draw request (a.k.a. payment request or application for payment) is prepared by the general. The general lists all the subs who are entitled to payment for work performed or materials supplied as of a particular date. The draw request lists the amount to be paid to each sub and it should also list any change orders which add items to or delete items from the contract amount. The amount to be paid for each category of work listed on the draw request must, as noted above, be posted on your spreadsheet. As with the cost breakdown, the draw request must contain an affirmation signed by the general that the information contained on the draw request is true and complete.

Each draw request for payment submitted by the general must be posted on the spreadsheet. By posting each draw request, the escrowee is able to determine the amount of funds (loan and owners) disbursed for each category of work and is therefore able to determine whether there will be sufficient funds to complete the improvement. If it appears after posting a draw that there will be a shortage of funds for any category of work, the escrowee should notify both the owner and the lender of the shortfall. It is then the joint responsibility of the owner and lender to direct the escrowee how or whether to proceed with the disbursement.

If a name appears on the draw request that does not appear on the spreadsheet, the general must be contacted for an explanation. The escrowee must determine if the general's explanation is acceptable, or whether the owner and/or lender should be notified of a potential problem.

The escrowee must receive appropriate lien waivers from all parties listed on the draw request. See below for a discussion of lien waivers.

Owner's Certificate or Authorization

The funds to be disbursed, whether they are loan funds or owner's equity, are the property of the owner. Therefore, funds should not be paid to the general without the written consent of the owner. The owner's certificate is the written authorization from the owner to the escrowee to disburse the funds requested by the general. The owners certificate must be signed by all owners {eg. Both husband and wife}.

The amount the owner authorizes to be paid should equal the amount requested by the general on the current draw. Again, any difference must be explained to the satisfaction of the escrowee. If the contract amount as shown on the owner's certificate disagrees with the draw request amount, or has changed since the last draw or cost breakdown, the escrowee should obtain copies of the written change orders that changed the contract amount.

Inspection Report

The escrowee should carefully review the report to determine that the work for which payment is requested matches the work found on site by the inspector. If the inspector suggests any holdbacks, the lender and owner instructions should either make the same holdback requirement, or acknowledge that no holdback will be required despite the inspection report. The inspection report is done for the lender. The escrowee will want to be certain that the lender has actually received the report, and is not relying on the escrowee to read and interpret the report on the lender's behalf.

Survey

Typically, with the first draw, the escrowee will receive a foundation survey. The foundation survey should be compared to all restrictions of record to determine if the foundation violates any setback requirements. This is particularly important if the lender has been given a comprehensive endorsement. If the structure violates a restriction, a neighbor could seek an injunction which would stop the project, and the lender could be covered on the policy as to that dispute.

Even if the foundation does not violate a setback requirement, the structure may violate after siding, roof overhang and gutters have been added. The escrowee should notify the owner and lender if there is any likelihood of a violation, and have the inspector review the plans to see if the building as built will violate.

The structure might also violate a zoning ordinance. However, because the title insurance policy provides no coverage as to zoning matters, and the escrow does not create a duty to review for zoning violations, the escrowee has no duty to determine if the zoning ordinance has been complied with.

The escrowee should receive an "as-built" survey with the final draw. As the name implies, this survey shows the completed project. Again, the escrowee should review the survey for violations of recorded restrictions. The survey should also be examined for all other typical survey matters, including encroachments onto neighboring property and onto easement rights. The lender may ask to have the survey exceptions removed on the pending disbursement endorsement issued with this draw. If this is done, all survey matters must be shown as exceptions.

Lien Waivers

Generally. When a person performs work on or supplies materials for an improvement, that person expects to be paid. While that person may commence a collection lawsuit against the general for what is owed, the person also possesses what are known as "lien rights" on the improvement itself. If the sub or supplier gives proper written notice to the owner, the sub/supplier may file a construction lien against the improvement. The Wisconsin construction lien law is contained in Chapter 779 of the Wisconsin Statutes. In very simplified terms, if the sub/supplier files a legally sufficient lien against the improvement, that lien may be foreclosed like a mortgage. The improvement can be sold to the highest bidder at a sheriff's sale with the proceeds divided up among the various lien claimants.

The following are the various dates that affect the validity of a construction lien:

1. Visible Commencement of work on the project – date on which lien rights accrue.
2. 60 Day Notice (aka Lien Notice) - must be given to owner within 60 days of when a contractor/subcontractor/supplier first begins work on the project.
3. 30 Day Notice (aka Notice of Intention to File Lien Claim) – must be given to owner at least 30 days before the lien is filed.
4. Construction Lien must be filed in the local Clerk of Courts Office no later than 6 months after a contractor/subcontractor/supplier completes work on the project.
5. Foreclosure action must be filed within two years of the date that the lien was filed. Lien expires after the two years if no action is filed. No extension is available.
6. Notices must be "*served on the Owner*".

In order to protect against construction liens being filed for funds that are disbursed, the escrowee should collect original executed lien waivers from the general and all subs and suppliers.

Supplier Waivers. While it is clear that waivers must be obtained from all the parties listed on the draw request, commonly called first and second lien claimants, invariably waivers must also be obtained from parties not expressly listed on the draw request. Those “unlisted” or “third tier” parties are the material suppliers. The escrowee should review each draw request and determine, based upon the escrowee’s experience, which of the subs listed on the draw must also submit a waiver from their suppliers. In most residential projects the subs will have the following material suppliers:

- Excavator – crushed stone
- Mason – cement, concrete block, bricks, crushed stone, steel beams
- Carpenter – lumber (both rough and finish)
- Plumber – pipes and fixtures
- Electrician – wire, conduit, fixtures
- Drywaller – drywall
- Painter – paint
- Carpet Installer – carpet
- Roofer – roof material

Some subs are large enough that they purchase their supplies in bulk (i.e. by the truckload or train car load). If the escrowee can verify that the sub takes its materials from its own fully paid inventory, then a supplier waiver is not necessary. However, a sub with an extensive paid up inventory is the exception and it is always prudent to ask for a supplier waiver.

Waiver Format. The actual physical form of the waiver is not crucial as long as the information contained on the waiver clearly shows who is waiving what lien rights. The waiver must contain:

- Owner’s name
- Project address (or name)
- Type of work performed or materials supplied
- Whether it is a partial or full waiver
- Original signature of the sub/supplier or its authorized representative

The escrowee must carefully examine the waiver to determine the authority of the person who signed it. The escrowee should always be watching for possible forged waivers, especially from subs and suppliers familiar to the escrowee.

Generally, only original waivers should be accepted. If a waiver is received via a facsimile, it is acceptable only if it can be verified that it was actually sent by the party waiving the lien rights and if the original will be delivered to the escrowee. Unless the escrowee would violate the disbursing agreement by accepting it, an invoice from a sub or supplier marked “PAID” can substitute for a waiver if the escrowee can verify that the sub or supplier was actually paid. However, this procedure should be limited to unusual situations even if the disbursing agreement would permit it. Also, a paid invoice alone is not sufficient proof that the sub or supplier was paid. Any invoice can be stamped “PAID”, and the subcontractor’s work to date may comprise more than one invoice.

Partial Waivers. Waivers may be limited in a number of ways. A waiver which at first appears to be “in full” may in fact be a partial waiver. The most common examples of waiver limitations are described below.

Limitations by Date. A waiver may say that it is for rights up to a particular date. In such cases, if a partial waiver is acceptable, the date on the waiver should be within two weeks or less of the date the draw request is submitted.

Limitation by Amount. A waiver may waive rights to a specific amount. If a partial waiver is acceptable, this type of limitation is acceptable as long as that amount is equal to the amount stated on the draw request for the particular sub/supplier. A common problem with this type of limitation is that the general contractor builds profit into the line item. The sub’s waiver, limited to the amount actually owed the sub, will show an amount less than the amount shown on the line item of the draw request. In that case, the escrowee should verify with the subcontractor that the amount waived is the amount actually owed to the sub.

Limitation by specified work. A waiver may contain a subtle limitation by listing the type of work or material being waived. If the waiver does not include all work performed by the sub to date and for which payment is requested, the waiver is probably insufficient. The most common example is when the sub is listed for several line items, but waives only one. In such cases, the waiver is acceptable as to the work waived, but another waiver must be received as to the balance of the work drawn for. {eg. Mason doing basement block, flatwork and brick veneer}

Limitation by Invoice Number. A waiver may state that it waives rights for certain identified invoices only. The result is that the waiver does not apply to work performed or material supplied under any invoice **not** listed. This type of waiver is often unacceptable, because the escrowee has no way of knowing whether or not the listed invoices are all of the invoices for the work to date.

Conditional Waivers. A waiver may state that it is given “on the condition of payment of \$x”. This is a conditional waiver. It is no waiver at all unless the amount specified is paid. Unless the disbursing agreement states otherwise, this type of waiver is not acceptable unless the escrowee itself is issuing the check to the sub and delivering it directly to the sub for the amount specified.

Trust Receipts. A trust receipt is a form of escrow agreement between the general contractor and sub, which says that the general may not deliver the waiver until it gives the sub the amount owed. The trust receipt is often attached to the waiver. A prudent sub will refer to the trust receipt right on the waiver so that the trust receipt cannot simply be torn off the waiver and the waiver submitted. If the escrowee detects from the waiver itself or some other information that a waiver has been supplied pursuant to a trust receipt, the waiver should be treated as a conditional waiver and not relied on.

Final or Full Waivers. At the time a line item is drawn for in full, the escrowee should receive full waivers from the subcontractor and supplier for that line item. If the inspection report says that a line item is complete, the waiver should be in full.

Be wary of a draw request which leaves a nominal amount of money on a line item, accompanied by a partial waiver. This could be an indication that the subcontractor is receiving a partial payment even though the work is complete and full payment is owed. The subcontractor could later file a lien for the unpaid balance of the work.

Prior to the final draw being disbursed, final unconditional waivers must be obtained from all the subs and suppliers listed on your spreadsheet.

Contractor's Completion Affidavit.

In addition to submitting a final lien waiver, the general must also submit an affidavit to the escrowee in which the general certifies that the project was completed on a particular date and that the only parties who had lien rights against the project are those listed on the spreadsheet, the draw request or on an exhibit attached to the affidavit.

Punchlist / Completion Escrows

A punchlist escrow may be required when a consumer purchases a completed house from a general contractor who still needs to finish some items such as landscaping and driveway. Commonly, the consumer buys the house in fall and the general agrees to return in spring to complete the necessary items.

In these cases, the escrowee should not simply hold the balance of the construction loan funds in the original construction escrow. Instead, a separate punchlist escrow should be set up which specifies the work to be done, the date by which the funds are to be disbursed, and the conditions under which the money will be disbursed to either buyer or general. The agreement should be very clear that the escrowee is not responsible if the amount of money held back is not enough to cover the work done.

Another common issue is the buyer's refusal to allow the release of money to the builder even though the stated work is done, because the buyer is unhappy with the quality of workmanship or other followup or warranty work. The escrow should clearly state the conditions under which the buyer can object to the release of funds to the builder.

1099 Reporting

IRS Regulations state that an escrowee disbursing construction funds who has "an oversight function with respect to a construction project" has a duty to report income disbursed on form 1099, unless the person being paid is exempt from reporting. Corporations are exempt from reporting. LLC's are not. An escrowee can receive significant fines for failing to report or reporting incorrectly.