

Restoration of Priority: Applying the Revised Notice of Termination Statute

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Title insurers are routinely called upon to insure loans on property before, during, and after construction. The priority of the loan is of paramount importance to the lender in every instance. Florida's Construction Lien Law, Sec. 713.13, F.S., contains the concept of the notice of commencement. The notice of commencement marks the beginning of construction and establishes a single point in time to which any liens filed against the property relate back. A notice of commencement is valid for one year (or longer if so provided). Its primary purposes are to create an equal playing field for all who work on a project and eliminate disputes over the priority of lienors' claims filed at various times during construction. A notice of commencement can create a challenge to the loan priority if it is recorded and unexpired prior to a mortgage in a current loan transaction.

When the work is complete, the owner can verify that the contractor and all its subcontractors and suppliers are paid in full by securing sworn payment affidavits and lien waivers. The significance of an open or unexpired notice of commencement is minimal if it is known there will be no more work on the project and proof that all who worked on it are paid in full is obtained. However, the situation is different when the work is ongoing and the owner needs to close on new or amended financing. The same notice of

commencement that established an earlier point in time for lien priority now presents a challenge to the priority of the new loan.

Assessing the Risk

The Fund has long recognized an inherent risk when balancing the rights of construction workers and suppliers with those who finance the improvements. The Construction Lien Law does not protect third-party lenders or their title insurers. Therefore, the Fund Member must use the tools within the Construction Lien Law when insuring new or modified loans during construction to minimize the risk of claims on the title policy. One tool that is especially useful in this situation is the notice of termination procedure set forth in Sec. 713.132, F.S.

Historically, the notice of termination process has been used to eliminate an open notice of commencement. The statute specifies the content requirements

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of a proper notice of termination and the prerequisites for its filing. It imposes an obligation to serve notice of the owner's intent to file a notice of termination of the notice of commencement on certain parties. Previously, the notice was only proper if the work was (a) complete, (b) or ceased before completion, and (c) all lienors were paid in full. Further, a notice of termination that was completed and properly served terminated the period of effectiveness 30 days after it was recorded or later if so stated.

New Legislative Changes

Effective Oct. 1, 2023, the provisions of Sec. 713.132, F.S., were changed in three significant ways. First, the notice of termination can now be filed at any time and is no longer limited to when construction is completed or work is ceased before completion. However, this does not dispense with the requirement that all lienors must be paid in full or pro rata. Second, the owner must serve notice on both the lienor who has a direct contract with the owner and those lienors who have timely filed a notice to owner. The newly inserted term "timely" now enlarges the class of parties to include those within their time to serve their notice to owner, even if its delivery to the owner is after the notice of termination is filed. This is of some significance since previously the owner needed only to serve notice of its intent to terminate on those from whom a notice to owner had been received prior to filing the notice of termination. According to the revised statute, the owner must also include a statement in the notice of termination that it will serve a copy of the notice of termination on each lienor who timely serves its notice to owner after the notice of termination is recorded. Third, the timeframe of the effectiveness of the termination is extended beyond the original 30-day period as to filers who timely serve their notice to owner after the notice of termination is recorded. The effective date of the notice of termination on these notice to owner filers is now 30 days after service of the notice of termination on such a timely filer. The practical effect of this change is that the notice of termination may terminate an open notice of commencement as to some lienors, but not all, during the initial 30 days after it is filed.

Going Forward

The demand to fund loans during construction remains high despite the change in the law. The risk associated with termination of an open notice of commencement during construction for loan restoration is much greater than when terminating the notice of commencement after all work is complete and the lienors are paid in full. Fund Members must consider new procedures to safely insure these loans when terminating an open notice of commencement during ongoing construction before replacing it with another notice of commencement recorded subsequent to the newly insured mortgage.

The traditional approach to termination of the open notice of commencement and restoration of lien priority was to (a) pause or cease construction, (b) pay all lienors in full through the date the work ceased, (c) terminate the notice of commencement, (d) record the new or amended mortgage (or mortgage modification), and then (e) refile a new notice of commencement. The date the work ceased served the dual purpose of establishing the end date of construction under the existing notice of commencement and defining the last date that payment was due for the work of each lienor. The change in the statute eliminates the need for work to cease or stop prior to completion when filing a notice of termination. Still, it does not change the requirement that all lienors must be paid in full or pro rata per Sec. 713.06(4), F.S. One practical challenge then is determining how to pay the lienors any amounts currently due if they do not stop working and continue to earn additional compensation. The Fund recommends establishing a specific payment date to create a target for paying all lienors any current amounts owed. This date should coincide with the loan closing to minimize the exposure of continuing charges for additional work the lienors perform. Upon payment, lienors' payment affidavits and lien waivers upon payment could then be collected and verified to satisfy this important step in the revised statutory scheme.

The second significant change to the statute, introducing the term "timely" to the ser-

vice by lienors not in privity with the owner, now must be considered when restoring priority.

The Fund Member restoring priority should implement a process that will include the owner/borrower's requirement to serve the notice of termination on all timely notice to owner filers, including those existing potential lienors who provide the notice to owner after the loan closing. Without this process, the termination may fail as to the potential lien claimants who subsequently provide the notice to owner. The statute already imposes this duty on the owner, but its noncompliance does not provide the title insurer any protection. One solution may be securing the owner's assurance at closing to provide the closing agent with notice of any new notices to owner and proof of service of the notice of termination on the new filers or a post-closing confirmation that no new notices to owner were received before the termination was effective. The change to the notice requirement and its possible effect warrants post-closing follow-up or confirmation, much like verifying the recording of a mortgage satisfaction, to confirm the necessary steps were taken and the termination was effective.

Another technique that may limit the risk of post-closing notices to owner is to have the owner secure the contractor's list of subcontractors and suppliers under Sec. 713.165, F.S., prior to closing. This list consists of all subcontractors and suppliers who have a contract with the contractor to furnish material or perform service with respect to the contracted improvements. This list must be accurate, or the contractor risks forfeiting its right to assert a lien on the property. Once obtained, all parties named on this list can be served with notice of the owner's intent to terminate the notice of commencement instead of limiting the owner's service list to only those lienors that previously provided a notice to owner. In this way, the service of notice by the owner will likely include all parties entitled to a potential lien, reducing the likelihood of any post-closing notices to owner under the prior notice of commencement.

Final Take

Restoring the priority of a loan over potential construction liens established by a recorded notice of commencement remains a constant necessity. Recently enacted changes to the notice of termination process under the Florida Construction Lien Law require an innovative approach to confirming the status of work and payments made to lienors on the project. Also, due care must be exercised when using the notice of termination process to confirm the insured loan has established priority and that the rights of lienors remain protected for future payment for labor, service, and materials rendered to the project. Members are encouraged to contact the Fund underwriting department for guidance with construction related issues. □