

The Risks Of Unnecessary Fla. Property Improvement Notices

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There's no doubt about it, the U.S. real estate market is strong. With low interest rates and low unemployment rates, it is not surprising that the National Association of Realtors included parts of Florida among the top 10 housing markets in the nation, predicted to remain robust over the next three to five years, especially for multi-family and single family housing projects.

As a result, a lot of developers are anxious to get their projects out of the ground while the going is still good. The first step in doing so is to begin site development activities like grading, paving and installing storm water systems, utility lines and other improvements that need to be in place before buildings can be constructed. All construction lenders want the developer to have skin in the game before giving them a loan to construct buildings, and starting site work in advance of a construction loan closing does that, in addition to accelerating the completion date for the project so it can get to market earlier.

It is not unusual for local building departments in Florida (both county and city) to require the recording of a notice of commencement by an owner of real property before issuing a permit for any improvements to the property. The NOC is intended to protect owners, construction lenders, general contractors and other parties who provide services or materials for construction projects, by promulgating information about the project, the identities of the principal participants and the scope of work, and establishing the start date of the work for the purpose of priority of liens.

While recording an NOC is appropriate for permits to construct most improvements, it is not appropriate in all circumstances, and can present significant issues if it is recorded when it is not required.

There are two significant exceptions from the requirement that an NOC be recorded when improving real property.

One exception applies if the direct contract price of the work is \$2,500 or less.[1]

The other exception applies if the work is of the type commonly called subdivision improvements or site work.[2] This consists of work required for the purpose of making the property suitable as a site for the construction of buildings. Examples of this, according to that statute, include “grading, leveling, excavating, and filling of land, including the furnishing of fill soil; the grading and paving of streets, curbs, and sidewalks; the construction of ditches and other area drainage facilities; the laying of pipes and conduits for water, gas, electric, sewage, and drainage purposes; and the construction of canals and ... the altering, repairing, and redoing of all these things.”

If a building department wants a developer to record an NOC for work that falls within one of these two exceptions, the applicable exception should be pointed out to the building department. Even when this is done, however, it is not uncommon for building officials to respond that they still want an NOC recorded as a condition to issuing a permit. If this occurs, the developer should point out Florida Statute Section 713.135(1)(e), which says that a permitting authority shall “not require that a notice of commencement be recorded as a condition of the application for, or processing or issuance of, a building permit.”

Why is this important? If an NOC is recorded for work done prior to a construction lender’s mortgage loan closing, the lender will require that it be terminated so as to preclude lien claims against the mortgaged property under the NOC that would relate back to the date the NOC was recorded and thereby prime the lender’s mortgage lien.

The procedure for clearing lien claims under Florida law is complicated and requires:

1. Stopping work;
2. Obtaining a final contractor’s affidavit from the general contractor confirming that the work to date was completed and all potential lienors paid;
3. Obtaining a list from the owner identifying all potential lienors who sent notices to the owner under the NOC;
4. Obtaining final lien waivers from all those who sent notices to the owner;
5. Recording a notice of termination of the NOC, with the general contractor’s affidavit attached;
6. Posting the notice of termination at the job site; and
7. Sending copies of the notice of termination by certified mail to the contractor and all parties who sent notices to the owner.

Even after doing all this, the notice of termination will not be effective to preclude further lien claims under the NOC until 30 days after recording, so it is possible for claimants to file liens within that 30-day period.

As long as the foregoing steps are taken and the owner indemnifies the title insurance company against any lien claims filed within 30 days after the notice of termination, a title company will typically insure that a construction lender’s mortgage will not be subject to lien claims arising under the prior NOC. Once the lender records its mortgage at the loan closing, the developer will then have to file a new NOC to complete the project.

Needless to say, all this can be a lot of brain damage for a developer, and can also require a fair amount of attorney fees. Additionally, if the general contract provided for retainage, it may have to be paid before it is due, or escrowed with the title insurance company, in order to allow the title company to insure over lien claims arising under the NOC.

The bottom line is that, if a developer is doing work on its property in advance of a construction loan closing, an NOC should not be recorded unless absolutely necessary. If the building department insists on it when a statutory exception applies, a developer should consider having their attorney speak to the local government's legal department about it to get the building department to back off.

Even if the recording of an NOC is appropriate before a loan closing, a developer should be careful to ensure that the NOC identifies a realistic date for it to expire in accordance with its terms, based on when the work is anticipated to be complete (failing which it will be valid for an entire year from recording). It is not unusual when an NOC is prepared to ignore the expiration date even if the work is expected to take a lot less time than a year. Once the expiration date passes, assuming the work is complete by then, it will not be necessary to terminate it using the complicated procedure cited above, since it terminates in accordance with its terms.

Finally, when recording an NOC before a loan closing, a developer should become familiar with the process required to clear lien claims, and make sure that they can live with the process and the length of time it will take to complete (i.e., sufficiently before the loan closing is required to occur).