BERGER SINGERMAN
FLORIDA'S BUSINESS LAW FIRM

DOES IT PAY TO USE JOINT CHECKS IN CONSTRUCTION?

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A joint check, also sometimes called a “two party” check, is payable to two parties. To cash the check, both parties must endorse the check.

Joint checks are used by owners to ensure general contractors will pay their subcontractors and material suppliers. Owners have a fundamental interest to ensure all subcontractors and suppliers are paid for their work because they may otherwise record construction liens against the owner’s property. Owners seek to ensure the payment of subcontractors and suppliers by issuing joint checks, made payable jointly to the general contractor and the subcontractor or material supplier.

Under a joint check arrangement, a contractor submits an application for payment itemizing the work performed by the subcontractors during that month’s payment period. The owner then issues checks payable jointly to the general contractor and the subcontractors whose work was listed on the application. This arrangement is advantageous to the subcontractor because it prevents the general contractor from using these monies to satisfy other obligations.

Joint checks are similarly used to ensure that second tier subcontractors (sub-subcontractors) and material suppliers are paid. This affords general contractors added insurance that monies dispersed are passed on to the appropriate subcontractor or supplier, reducing the risk that a subcontractor retains or withholds the payment due to the supplier, and the supplier records construction liens against the owner’s property or makes a claim against the general contractor’s payment bond. The supplier may initiate a joint check arrangement if, for example, the subcontractor is in ?nancial trouble, lacks assets or if has never done business with the subcontractor before.

Although joint checks are commonly used in the construction industry, joint checks may present several legal complications. The endorsement of a joint check may create a legal presumption that the co-payee has been paid the full amount of the check, even if the other co-payee has withheld part or all of the funds.

The Joint Check Rule

Under the “joint check rule”[i], when a joint check is made payable to joint payees (e.g., general contractor and subcontractor, or subcontractor and its sub-subcontractor or material supplier), absent an agreement regarding the allocation of the proceeds of the joint check, the contractor or supplier who endorses the check, is presumed to have received all sums owed to it as of the date the check covers, even though it may have received only part or none of the amounts owed.

The basis of the joint check rule is that a joint check arrangement protects owners and general contractors by eliminating potential lien claims and protect suppliers and laborers by ensuring payment.

Issues Raised By Joint Check Arrangements

Joint check arrangements raise many issues. One issue to consider is whether one of the construction parties can unilaterally institute the joint check arrangement. Without a contractual right, a general contractor cannot unilaterally satisfy its payment obligations by issuing joint checks if the subcontractor or supplier has not agreed to the arrangement. To do so, may be a breach of contract.

Another issue with joint checks is how the joint check proceeds are to be allocated between the payees on the check. It is the duty of the co-payee of the joint check to determine the intention of the issuer of the check as to the allocations of the proceeds of the joint check. This means that a co-payee of a joint check should obtain an agreement or instructions from the issuer of the check prior to endorsing the check. The existence of a written agreement as to the allocation of the proceeds negates the presumption created by the joint check rule that the co-payee who signs a check has been paid everything up to the date the check is endorsed.

A third issue that arises with joint check arrangements is whether endorsing a joint check operates to release or waive lien rights. Some courts have held that the owner or general contractor is protected against liens by anyone named on a joint check, up to the amount of the check, even if they did not obtain waivers of lien.

A further issue to consider is when a joint payee negotiates a joint check without the proper endorsements and then does not pay the other joint payee the proceeds it is owed. For example, a joint payee may forge the other payee's endorsement and wrongfully deposit the check or may submit the check for negotiation without endorsement. If a payee on a joint check wrongfully endorses and cashes a joint check, the issuer of the check may still be liable to pay the party that received none of the proceeds of the check. If a bank accepts a joint check endorsed by only one of the two joint payees, then the bank, the payor, and the payor's surety (if any) may be liable to the non-signing payee.

Issuing joint checks can also expose the general contractor to independent liability to pay lower tier subcontractors and suppliers. Some courts hold general contractors liable for a subcontractor's obligations to a supplier when executing a joint check agreement. Subcontractors also may be at risk. A joint check agreement between a subcontractor, sub-subcontractor and supplier, coupled with an assurance of payment by the subcontractor, may make the subcontractor a guarantor to supply all of the required materials for a project. Careful drafting of joint check agreements is therefore essential.

Finally, joint check arrangements can raise bankruptcy-related issues, including whether a debtor/joint payee has suf?cient interest in joint check proceeds to establish a preference claim for payments received within ninety days of the ?ling of the bankruptcy petition.

Conclusion

Joint check arrangements are common in the construction industry because they offer many advantages. If you are an owner or a general contractor, issuing joint checks can be an effective way to ensure that a subcontractor or material supplier is paid. If you are a sub-subcontractor or supplier, joint checks can be a form of payment security because they signi?cantly reduce the opportunity for a subcontractor to withhold some or all of money due to you. Joint checks, however, can create many problems. A carefully drafted joint check agreement and having a clear understanding of the legal rami?cations that can result from joint checks can help avoid the pitfalls of joint checks.

Should you have any questions or concerns about your construction contracts, please do not hesitate to reach out to Jeffrey S. Wertman or other team member on the firm's Construction Team.

[i]The joint check rule is recognized in some, but not all jurisdictions. To avoid the consequences of endorsing a joint check, a subcontractor, sub-subcontractor or material man can protect itself by refusing to endorse the joint check until assured by escrow or other arrangement that it will recover its rightful share of the check.

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