

# Holdback Instructions/ Agreements 101+

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Presented by:

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# Introduction

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Holdbacks in real estate transactions serve as a form of financial security or insurance against potential post-transaction issues or concerns. They protect the interests of buyers and sellers as well as title insurers by providing funds to address repairs, legal disputes, or other unforeseen expenses.

# What Is an Escrow Holdback?

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- An escrow holdback involves placing a portion of transaction funds into an escrow account, where they are held by a neutral third party, such as Stewart Title Guaranty Company. These funds are not released until specific conditions or milestones outlined in the agreement are met.
- Escrow holdbacks are commonly used in real estate, mergers and acquisitions, construction projects, and other business deals where there is a need for added financial security.

# The Basics of Holdbacks

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- **Holdback Amount:** This is the specified amount that is withheld at the close of the transaction by the escrow holder until certain conditions are satisfied. The amount can vary depending on the nature of the issue.
- **What are the funds held for?** Specifying what the issue is to be rectified as a condition of releasing the funds.
- **Conditions to Release:** Holdbacks are typically tied to specific conditions that must be met, such as the completion of repairs, receipt of final permits, Release of a judgement, etc.
- **Time Frame:** A deadline is usually set for when the conditions must be met.

# The Pros of Using Escrow Holdbacks

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## 1. Enhanced Financial Security

One of the primary benefits of an escrow holdback is the financial security it provides. By holding funds in escrow, parties can ensure that obligations are met before the money is released.

### For example:

- In a real estate transaction, a holdback can ensure that the seller completes agreed-upon repairs.
- In a business sale, a holdback can verify that the seller fulfills performance clauses or transitions assets.

This layer of protection builds trust and reduces the risk of disputes.



# The Pros of Using Escrow Holdbacks

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## 2. Neutral Oversight

Escrow holdbacks are managed by a neutral third party, such as the escrow holder, ensuring impartial oversight of the funds. This prevents either party from having undue control over the money, fostering fairness throughout the process.



# The Pros of Using Escrow Holdbacks

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## 3. Flexibility for Various Scenarios

Escrow holdbacks are incredibly versatile and can be used in many situations, including:

- Addressing incomplete construction or repairs.
- Resolving disputes over contract terms.
- Ensuring compliance with warranties or maintenance agreements.

This adaptability makes escrow holdbacks a reliable solution for both simple and complex transactions.

# The Pros of Using Escrow Holdbacks

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## 4. Minimized Disputes

By clearly defining the conditions for fund release, escrow holdbacks help minimize misunderstandings or disagreements between parties.

Everyone knows what is required to fulfill the terms of the agreement, which helps avoid unnecessary legal battles.





# The Pros of Using Escrow Holdbacks

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## 5. Protection Against Unforeseen Issues

Escrow holdbacks provide a safety net against unforeseen challenges, such as delays in obtaining permits, unexpected repairs, or non-compliance with contractual obligations. This ensures that the transaction can move forward without unnecessary delays or risks.

# The Cons of Using Escrow Holdbacks

## 1. Added Complexity

While escrow holdbacks offer many benefits, they can add complexity to a transaction. The parties involved must agree on the conditions for releasing funds, which can take time to negotiate and finalize.



# The Cons of Using Escrow Holdbacks

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## 2. Potential Delays

Since funds are only released when specific conditions are met, there may be delays if those conditions are not fulfilled on time. For instance, a contractor may take longer than expected to complete repairs, or a seller might need extra time to meet performance milestones.

To mitigate delays, it's essential to establish realistic timelines and manage the process efficiently. Thus, calendaring check-ins with the parties.



# The Cons of Using Escrow Holdbacks

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## 3. Associated Costs

Escrow holdbacks can come with administrative fees, which may be seen as an additional expense in a transaction. However, these costs are typically outweighed by the financial security and peace of mind that escrow holdbacks provide.

Make sure all parties agree with any additional costs involved with Holdback, and that the escrow holder's fee is stated in the Holdback Agreement that all parties execute.

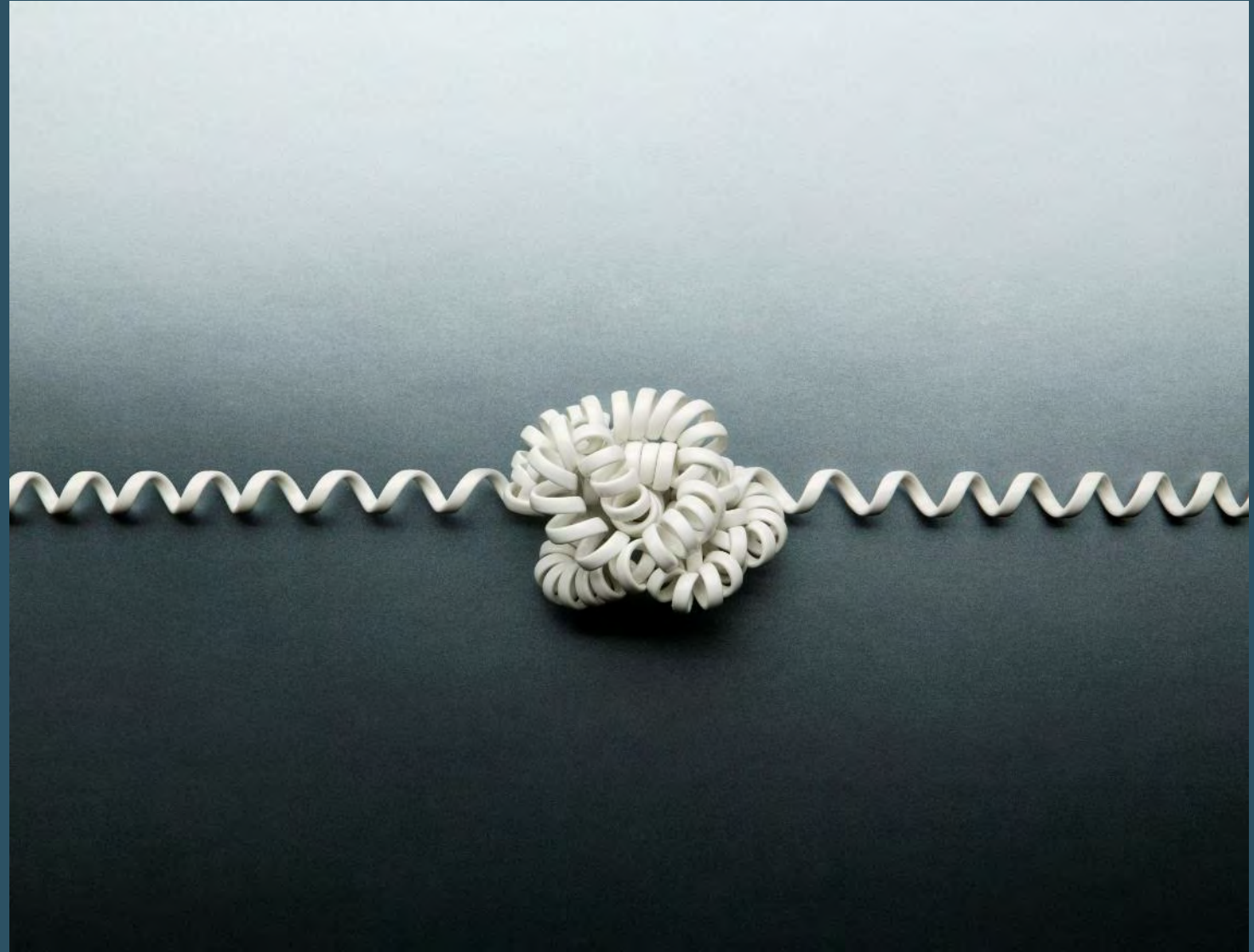


# The Cons of Using Escrow Holdbacks

## 4. Risk of Miscommunication

If the terms of the escrow holdback agreement are not clearly defined, there is a risk of miscommunication between parties. This can lead to disputes or delays in fund release.

To avoid this, it's crucial to prepare clear and comprehensive agreements.



# How Holdbacks Are Structured

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The structure of a holdback agreement can vary depending on the specifics of the transaction. However, there are some common elements that are typically included in a holdback arrangement:

# Determining the Holdback Amount

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The amount of the holdback is usually based on the estimated cost of completing the work or resolving the issue. In some cases, an additional buffer may be included to cover any unforeseen expenses.

# Setting Clear Conditions

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The conditions under which the holdback will be released must be clearly defined. This includes specifying what work needs to be completed, any standards or approvals required, and the deadline by which these conditions must be met.



# Establishing a Deadline

A deadline is usually set for the completion of the work or resolution of the issue. If the conditions are not met by this deadline, the Holdback Agreement needs to specify what is then to take place. Which can include the other party receiving the holdback funds to use them to address the issue directly.



# Legal Considerations

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The holdback agreement should be documented in writing and included as part of the purchase agreement or a separate contract. It's also advisable that if the parties do not have legal counsel involved in the transaction, that they have the right to seek legal representation to review the agreement to ensure that the holdback is structured as they anticipate and protects their interests.

# Disputes Over Completion

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One of the primary risks associated with holdbacks is the potential for disputes over whether the conditions have been met. If the buyer and seller disagree on the quality or completeness of the work, it can lead to delays in releasing the funds and even legal disputes. Thus, it's imperative that Holdback Instructions have very specific conditions for the release of funds and then further specific instruction, as to what will take place in the event of a dispute.

# Delays in Receiving Funds

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For sellers, a holdback can mean a delay in receiving the full sale price. This can be particularly problematic if the seller is entering into a 1031 tax deferred exchange. Make sure to discuss the terms of the holdback with the seller's exchange accommodator, to ensure that all parties are aware of the timelines and any tax consequences that the funds may be subject to, in the event the release of the funds falls outside that time frame.



# Additional Costs

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If the holdback amount is insufficient to cover the cost of the required work, the agreement needs to clearly specify which party will be responsible for the additional cost and if payment of that additional cost is to be deposited into the escrow account or paid outside of the escrow account directly to the party due to receive the funds.

# Agreements drafted by outside parties- The importance of red lining:

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It's common for counsel representing the principals in a transaction to prepare and negotiate a proposed Holdback Agreement that gets deposited into escrow. However, always keep in mind that the escrow holder is also a party to the agreement and as such has the right and moreover, the obligation to review a draft of the proposed Holdback Instructions before execution. As the escrow holder, it's imperative that you confirm that the agreement contains all the specific requirements discussed above. As the escrow holder, you are a party to the agreement and have the right to require revisions if the instructions are ambiguous in any way, or do not contain sufficient information.

# EXAMPLE HOLDBACK AGREEMENT

File No. [REDACTED]

Date: \_\_\_\_\_, 20\_\_

Stewart Title Guaranty Company  
NCS Office Address

Attn: \_\_ (escrow officer) \_\_\_\_\_

RE: [REDACTED] (property address)

Ladies and Gentlemen:

Reference is made to the \_\_\_\_\_, dated \_\_\_\_\_, 20\_\_ (the "Agreement") between (seller) [REDACTED] ("Seller") and [REDACTED] ("Buyer") regarding the premises captioned above and more particularly described on Exhibit A attached hereto. Buyer has this day deposited with Stewart Title Guaranty Company ("Escrow Agent") the sum of \$ \_\_\_\_\_ (the "Escrowed Funds").

Escrow Agent shall hold the Escrowed Funds subject to the following terms and conditions:

1. Escrow Agent is not a party to, and is not bound by, or charged with notice of, any agreement out of which this escrow may arise, other than the terms and provisions of this escrow letter.
2. A lis pendens was recorded as Instrument No. \_\_\_\_\_ of the Official Records of \_\_\_\_\_ County, California (the "Official Records") on \_\_\_\_\_, 20\_\_ (the "Lis Pendens"). Seller agrees to obtain a certified copy of a release/withdrawal of Lis Pendens in recordable form (the "Release") and to deliver said Release to Escrow Agent within ninety (90) days of closing (the "Delivery Period"). Upon Escrow Agent's receipt of the Release within the Delivery Period, Escrow Agent shall notify Buyer and Seller of said receipt and will immediately submit the Release for recording in the Official Records, without any further instruction from either Seller or Buyer. Upon Escrow Agent's receipt of confirmation of recording of the Release, Escrow Agent shall disburse the Escrowed Funds to Seller, without any further instruction from Buyer. No additional consent or approval from Buyer shall be required for Escrow Agent to disburse the Escrowed Funds to Seller, once Escrow Agent has received confirmation of the recording of the Release. Escrow Agent shall provide notice of the recording of the Release to Seller and Buyer via electronic mail to the notice addresses set forth below. If the Release is not delivered to Escrow Agent within the Delivery Period, Escrow Agent shall disburse the Escrowed Funds to Buyer within ten (10) days of the expiration of the Delivery Period. No additional consent or approval from Seller shall be required for Escrow Agent to disburse the Escrowed Funds to Buyer, in the event Seller does not deliver the Release to Escrow Agent within the Delivery Period. Escrow Agent shall disburse the Escrowed Funds to either Seller or Buyer, subject to the terms and conditions set forth herein, pursuant to the

# EXAMPLE HOLDBACK AGREEMENT

recipient's instructions for method of payment, (i.e., check payment or wire transfer).

3. Escrow Agent is acting solely as a stakeholder and depository as an accommodation to Buyer and Seller and is not responsible or liable for any matter or loss arising out of Escrow Agent's conduct or omissions hereunder, except to the extent arising from its gross negligence or willful misconduct. Escrow Agent is not responsible or liable for the sufficiency, correctness, genuineness, or validity of the subject matter of this escrow letter, or for the identity or authority of any person executing any documents or instruments in connection herewith.
4. Buyer and Seller agree to jointly and severally indemnify, defend, and hold harmless Escrow Agent from and against any loss, costs, claims, damage, liability, or expense, including, without limitation, any and all court costs and attorneys' fees and expenses (collectively, "Expenses") incurred by Escrow Agent in connection with or in any way arising out of this escrow letter, except to the extent such Expenses arise from Escrow Agent's gross negligence or willful misconduct. Escrow Agent may, at its own expense, consult with legal counsel in the event of any dispute or questions as to the construction of any provisions hereof or its duties hereunder, and it shall have no liability to any party as a result of any action or inaction taken in accordance with the opinions or instructions of such counsel. The parties acknowledge and agree that Escrow Agent's duties are ministerial only and Escrow Agent does not provide any tax, accounting, or legal advice.
5. Escrow Agent shall be entitled to act or rely upon, and Escrow Agent shall have no liability as a result of Escrow Agent acting or relying upon, the genuineness and validity of any written notice, request, waiver, consent, certificate, receipt, authorization, power of attorney, or other document Escrow Agent shall receive from any party hereto.
6. In the event that (a) Escrow Agent receives contradictory instructions from the parties hereto, or (b) there is any dispute between Seller and Buyer as to any matter arising under this escrow letter, or (c) there is any uncertainty as to the meaning or applicability of the provisions hereof or any written instructions received by Escrow Agent pursuant hereto, Escrow Agent may, at its option, continue to hold the Escrowed Funds pending resolution of the matter or deposit the Escrowed Funds with any appropriate court in the state of California at the cost and expense of Buyer and Seller, jointly and severally. Upon making such deposit with the court, Escrow Agent shall thereupon be discharged and released from any and all liability with respect to the Escrowed Funds. Escrow Agent may dispose of the Escrowed Funds in accordance with a court order and shall have no liability to any party for acting in accordance with any such court order.
7. The Escrowed Funds received by Escrow Agent will be deposited with other escrow funds in one or more non-interest-bearing escrow accounts with a financial institution selected by Escrow Agent. Escrow Agent may be eligible to participate in a program whereby it may receive (a) favorable loan terms and earn income from the deposit, and (b) other direct or indirect benefits from its financial institution by reason of the deposit and/or the maintenance of such accounts. Escrow Agent shall have no obligation to account to any party in any manner for the value of, or to pay to any party, any benefit received by Escrow



# EXAMPLE HOLDBACK AGREEMENT

Agent from its financial institution.

8. When agreed or directed by the parties hereto, deposits made pursuant to these instructions may be further invested in an interest-bearing account with a financial institution selected by Escrow Agent, on behalf of any party or parties hereto, provided that any direction to Escrow Agent for such investment shall be in writing and contain the consent of all other parties to this escrow, together with a completed, signed W-9 Form. Escrow Agent is not responsible for levies by taxing authorities based upon the taxpayer identification number used to establish this interest-bearing account.
9. Escrow Agent has no liability in the event of failure, insolvency, or inability of a financial institution to pay said funds or accrued interest upon demand for withdrawal.
10. Upon delivery of the Escrowed Funds in accordance with the terms hereof, Escrow Agent shall be discharged and released from any and all liability with respect to the Escrowed Funds.
11. This escrow letter may only be modified or supplemented by an instrument in writing executed by duly authorized representatives of Escrow Agent, Buyer and Seller. This escrow letter may be executed in one or more counterparts, each of which shall be deemed an original, but all of which shall constitute one and the same instrument.

Very truly yours,

**SELLER:**

\_\_\_\_\_  
a \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Its: \_\_\_\_\_

Taxpayer ID No.: \_\_\_\_\_  
Address: \_\_\_\_\_  
\_\_\_\_\_

# EXAMPLE HOLDBACK AGREEMENT

BUYER:

a \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Its: \_\_\_\_\_

Taxpayer ID No.: \_\_\_\_\_

Address: \_\_\_\_\_

\_\_\_\_\_

Accepted and Agreed to:

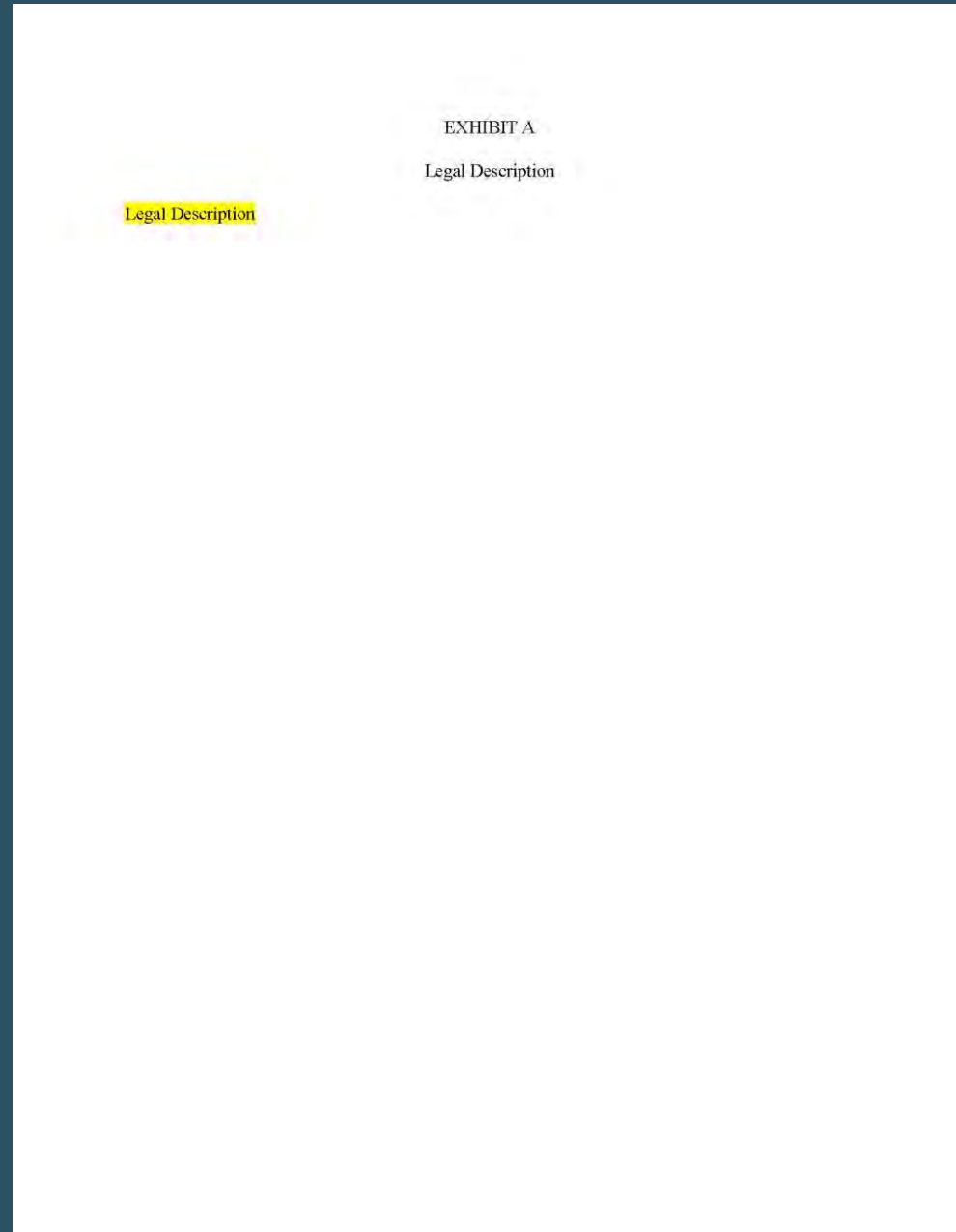
STEWART TITLE GUARANTY COMPANY

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

# EXAMPLE HOLDBACK AGREEMENT



# Thank you. Questions?

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## **Stewart Title Guaranty Company**

National Commercial Services

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Concord, CA 94520

[stewart.com/commercial](http://stewart.com/commercial)