

# “The Often Overlooked Dangers of Lender’s Assignment and Consent Agreements”

A MyProfessionalNet Professional Education Webinar

Presented By:

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# Company Description

- ▶ Thompson Becker, LLC provides legal services to architects, engineers, land surveyors and related construction professionals. Whether your needs are contract reviews, liability consultations or litigation support, our firm strives to provide your firm the most competent legal representation possible, so that you may concentrate on effectively and profitably running your business.

# Agenda

This presentation will focus on the often overlooked and misunderstood agreements issued by lenders, and explain how certain provisions, or even a single word, have the potential to expose your firm to unanticipated liability and/or can jeopardize the professional liability coverage purchased by your hard-earned premium dollars.



# Trending or More of the Same?

- ▶ In today's economic climate, financial institutions want to know the project is good security for their sizeable loans.
- ▶ More and more architects and engineers are being asked to address client issues relative to financing, such as a lender's request for an assignment and certification.
- ▶ Every architect and engineer should be knowledgeable on these issues and approaches.



# Contractual Obligations v. Practical Considerations

- ▶ A design professional may not have a contractual obligation to consent to an assignment, provide a certification, or furnish future services to a lender.
  - ▶ In fact, the professional services contract may contain a provision prohibiting such an assignment or may be silent on the issue altogether, thus enabling a negotiation of acceptable assignment terms.
- ▶ Practically, however, most design professionals proceed with the assignment to accommodate the client regardless of contractual protections.



# Current AIA Position in B101-2017

- ▶ 10.3 The Owner and Architect, respectively, bind themselves, their agents, successors, assigns and legal representatives to this Agreement. Neither the owner nor the Architect shall assign this Agreement without the written consent of the other, except that the Owner may assign this Agreement to a lender providing financing for the Project if the lender agrees to assume the Owner's rights and obligations under this Agreement, including any payments due to the Architect by the Owner prior to the assignment. *[underscore added in 2017]*
- ▶ 10.4 If the Owner requests the Architect to execute certificates, the proposed language of such certificates shall be submitted to the Architect for review at least 14 days prior to the requested dates of execution. If the Owner requests the Architect to execute consents reasonably required to facilitate assignment to a lender, the Architect shall execute all such consents that are consistent with this Agreement, provided the proposed consent is submitted to the Architect for review at least 14 days prior to execution. The Architect shall not be required to execute certificates or consents that would require knowledge, services or responsibilities beyond the scope of this Agreement, *or in the sole judgment of the Architect, would increase the Architect's contractual or legal obligations or risks, or the availability or costs of its professional or general liability insurance.*

# Negotiating the Consent and Certificate

- ▶ Lender's consents and certificates are not uniform. A few seek, in varying degrees, to assume the underlying contract and acknowledge the design professional's proper role in construction. Most are wholly self-serving adhesions.
- ▶ A decision by a design professional to agree to an assignment does not mean that a design professional also has to extend its risk by signing an onerous consent, providing an unfair certification to the assignee, or otherwise extending rights to the lender that are not envisioned by the contract.



# Issues and Concerns

- ▶ When a client's financing requires assigning contractual rights to a lender who in turn requires consent and certification of project information from the design professional, there are numerous and varied concerns to address depending upon the form used by the lender, including:
  - ▶ 1. Whether the design professional is comfortable with providing services to an unknown client - both before and after the assignment.
  - ▶ 2. Whether the design professional will be properly compensated for services after a loan default.
  - ▶ 3. Whether the instruments of services could be used in an unmanaged situation thus increasing the risk of meritless claims against the design professional.
  - ▶ 4. Whether the design professional is extending its liability through its certification or statements to the lender.
  - ▶ 5. Whether the assignment contains express warranty or guarantee language.

# Is The New Client Willing To Assume The Obligations Of The Original Client?

- ▶ Revise any provision that seeks to assign the benefits but avoid the obligations of the agreement, contrary to section 10.3:
- ▶ “The undersigned Engineer acknowledges the assignment by Owner to Lender, as additional security under a Construction Loan Agreement, of all of the rights ~~(but not obligations)~~ and obligations of Owner in the Agreement between Owner and Engineer pertaining to the construction of the improvements described in the Plans (the “Improvements”). Engineer hereby consents to and agrees to be bound by such assignment.”

# Protecting Your Fee and the Plans

- ▶ When the Lender wants the option to terminate your services upon default.
- ▶ “Irrespective of Engineer being further actively employed, Lender and Lender’s Successors shall be entitled to use for the completion of the Improvements and Plans prepared by Engineer for the project, ~~without further cost to Lender or Lender’s Successors~~ provided Engineer has been fully paid past sums for services rendered on the project and Lender releases Engineer from future liability and defends and indemnifies Engineer from all claims arising out of Lender’s use of the Plans.”



# Protecting Your Fee and the Plans

## pt. 2

- ▶ When the Lender wants to continue with your services but not pay fees owed by the client, contrary to 10.4:
- ▶ “Lender shall have the rights of Owner under the Architect Agreement, including the right to use the Plans and the ideas, designs and concepts contained therein in connection with the completion of the Improvements provided Architect continues performance under the Architect Agreement and is paid all amounts for architectural fees incurred for services performed after default, as provided for in the Architect Agreement, and any overdue fees, costs and expenses at the time Borrower requests the continued performance of Architect.”



# You Want Us to Do What?

- ▶ Delete any service or obligation not in the client agreement.
- ▶ Ex. “Engineer shall provide Lender promptly in each case with (a) any information regarding defects in workmanship or materials which come to Engineer’s attention, (b) any deviations or variations in construction of the project from the Plans, (c) any information Engineer may have regarding any defaults by Owner or any contractor or subcontractor under any construction contracts, and (d) any claims of non-payment by any person furnishing labor or material in connection with construction of the project.”

# And what else...?

- ▶ “The undersigned shall not make any changes in the Plans without the prior written consent of Lender and shall immediately notify Lender of any changes of which undersigned may become aware.”
  - ▶ Strike this.
- ▶ “Architect agrees to give Lender written notice of any material defaults by Borrower under the contract, and to give Lender, at the sole option of Lender, the right to cure any material defaults by Borrower under the Contract within ~~14~~ 60 days (or such longer period of time, if any, as permitted in the Contract for the curing of any such defaults) after receipt by Lender of written notice of such material defaults, ~~during which time Architect will not exercise any remedy available under the Contract, at law, or in equity, arising from such default by Borrower until Lender shall have had the opportunity to cure such default.~~”

# Lien Rights

- ▶ “The undersigned hereby waives and released all Lien rights under the mechanics’ lien or other similar laws in connection with all services performed on the Project, including the preparation of plans and specifications for and supervision of said work.”
- ▶ The current NJ Construction Lien Law prohibits waivers at NJSA 2A:44A-38

# Certification Forms: Why “certify” is almost always a bad word!



# Certification Forms

- ▶ **“We hereby certify...”** Straight off, you are asked to certify what is written in the balance of certificate. A certification is not casual commentary. **“Certify”** is a word with a specific meaning, and it is for that meaning the lender chose it. To **“certify”** means to establish a thing as a fact. **“Certify”** specifically supplants matters of opinion.
- ▶ Your professional liability insurance company will not like the “certification,” and it would likely decline coverage for any claim based on certification.
- ▶ One of the additional consequences of establishing a thing as a fact is to state a warranty or guarantee of truth. Your professional liability insurance policy excludes warranties and guarantees. So, avoid any uninsurable risk from any express warranties or guarantees as might be included in an unqualified certification.
- ▶ Sample coverage exclusion: “We will not defend or pay under this Policy for any claim arising out of your alleged liability under any written or oral contact or agreement, including but not limited to express warranties or guarantees.”

# ~~Certify~~

- ▶ Lenders, design professionals, and the clients of design professionals should acknowledge the design professional can and should only offer a professional opinion that relates to the information available through his or her scope of services, and beliefs based on that information and the application of his or her knowledge.
  - ▶ Any reliance upon information provided to the design professional by the owner or third parties should be identified as such. See section 3.1.2 of B101-2017.
- ▶ Strike “certify.” Use: “In the architect’s professional opinion...” or “We hereby opine...” or “It is our opinion that...”
- ▶ In the event the word “certify” cannot be expunged, asterisk (\*) the words “Certificate” and “certify” and insert the following footnote:
  - ▶ \*The word, “certify”, as used in any of its forms herein, is an expression of a professional opinion only and shall not be construed or understood to be a statement of fact, a warranty, or a guarantee of any kind, expressed or implied.

# Examples

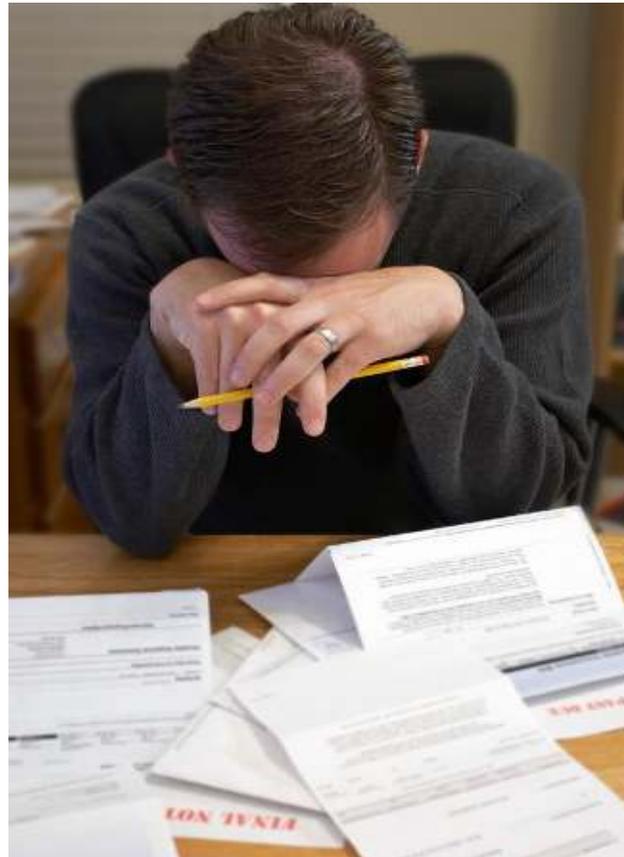
- ▶ Ex. “We certify that all permits and approvals, with the exception of building permits, necessary for the construction of the Project have been obtained.”
- ▶ Ex. ~~“We certify that~~ In our professional opinion, and based upon information provided by Owner, the permits identified on Exhibit A, attached hereto ~~and incorporated herein by this reference~~ are the only federal, state or local permits or approvals required for the construction of the Improvements that are applicable to and within the architect’s scope of services and have been obtained by or on behalf of the Owner, and except as otherwise noted, each has been validly issued by the appropriate authorities. However, architect does not represent that Exhibit A is a complete list of every permit and approval obtained by or on behalf of the Owner for the project or still required for the project.”

# More Examples

- ▶ Ex. ~~“We hereby certify~~ It is our professional opinion that upon completion of the Improvements substantially in accordance with the Plans the Improvements will substantially comply with the Plans and ~~all applicable~~ those building codes and regulations, including, without limitation, federal, state and local laws, statutes, regulations, and ordinances applicable to and within the scope of the Architect’s services provided under the Contract.”
- ▶ Ex. ~~“We certify~~ the Plans have been prepared and will continue to be prepared in accordance with customary professional standards of architectural practice for projects similar to the Improvements, such that when finalized, the Plans will be complete and adequate, in the Architect’s professional opinion for the construction of the Improvements.”
- ▶ Ex. “We are familiar with the prior uses of the Land, the surrounding land, and the building site, and the history is such that we certify no wastes, toxins, pollution, or contamination adversely affecting the intended use are present on the site or in the soil or ground water.”

# Inducement or Reliance Provisions

- ▶ “Engineer is executing this Consent, Agreement and Certificate to induce Lender to advance funds under the Loan Agreement, and Engineer understands that Lender would not do so but for Engineer’s execution and delivery of this Consent, Agreement and Certificate.”
- ▶ The lender needs some hook to convince a judge to enforce this certificate on its behalf and against you.
- ▶ Strike these provisions! Do not acquiesce to the pretense that the lender’s decision is based primarily on the consent and certification unless there is a recognition of this assumed risk through compensation to the design professional for this unnecessary and significant risk.



# A WORD ON TIME AND PRESSURE



- ▶ Paragraph 10.4 of AIA B101 limits the architect's duty to sign certificates to those which require knowledge and services within the scope of (your) agreement and gives the architect at least two weeks to review and prepare an acceptable form.
  - ▶ Your contract with your client should not lack similar protection.
- ▶ A client and the lender may state that without immediate consent to the assignment and issuance of accompanying certifications by the design professional, the loan will not be issued.
- ▶ Don't be pressured into signing the lender's form!

# Closing Statements

- ▶ Include appropriate language in your client agreement.
- ▶ Negotiate a fair consent/certificate with Lender.
- ▶ Do not certify!
- ▶ Do not be pressured!
- ▶ Seek advice.

# Questions?

Thank you!

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