

An Overview of Consent to Assignment Agreements

By Gail S. Kelley, P.E., Esq.

Design agreements often stipulate that neither the owner nor the engineer can assign the agreement without the consent of the other party. As a result, the engineer may be asked to sign a "Consent to Assignment" (sometimes referred to as an "Acknowledgement and Consent") from the bank providing the construction loan. A typical consent form requires the engineer to agree that the design agreement can be assigned to the lender. The assignment will actually occur at the time the loan is closed; however, the assignment is conditional in the sense that the lender can only assume the design agreement if the owner defaults on the loan.

If the owner defaults and the lender takes over, the lender's chances of finding a buyer for the project are significantly better if the buyer has the option of assuming all of the key contracts for the project. Thus the lender may ask the contractor, the engineer, and the other key design consultants to consent to an assignment of their contracts.

While Consent to Assignment requests are common, particularly on large projects, there is no standard form. The consent should be read carefully and preferably reviewed by the engineer's legal counsel. Although the lender cannot assume the design agreement unless the owner defaults, the forms used by many banks contain provisions completely unrelated to the design agreement. Engineers who are not careful may find that they have given up valuable rights or agreed to unreasonable obligations even if there is no default by the owner.

General Structure of a Consent to Assignment

There are several different ways to structure a consent agreement. Sometimes it is structured as an agreement between the owner (the borrower), the engineer, and the lender, with all three parties signing. For example:

This CONSENT TO ASSIGNMENT (this "Agreement"), dated as of _____, by and among _____, (the "Borrower"), _____ (the "Engineer"),

and _____ as agent for the Lenders (together with its successors in such capacity, the "Agent").

Alternatively, it may be structured as an agreement between the owner and the engineer, with the lender as a third-party beneficiary.

This CONSENT TO ASSIGNMENT of Engineer's Contract (this "Agreement") is made as of _____ by and between _____ ("Borrower") and _____ ("Engineer") for the benefit of _____ ("Lender").

It may also be structured as an agreement between the engineer and the lender:

This CONSENT TO ASSIGNMENT (this "Consent") is dated as of _____ by _____ ("Engineer") to _____ ("Lender").

Finally, although less commonly, it may simply be written as what it is, which is a one-sided agreement under which the engineer agrees to do, or not do, certain things:

The undersigned, as Engineer under the Design Agreement dated as of _____ (the "Design Agreement") between _____ ("Borrower") and the undersigned, which is one of the contracts referred to in the Assignment of Agreements ("Assignment") between Borrower and _____ (the "Lender"), agrees that upon receipt of notice from Lender that a Default has

occurred under the Assignment, it will perform all of its obligations under the Design Agreement for the benefit of Lender.

Regardless of how the consent is structured, the intent is to ensure that if the owner defaults on its loan and the lender takes over, the engineer will continue to provide the services called for under the design agreement if requested to do so. The agreement typically also gives the lender the right to use the engineer's Instruments of Services to complete the project with another engineer.

Payment of Outstanding Obligations

If the owner has defaulted on its loan, it is likely to be behind in its payments to the engineer. Thus, a key issue is the lender's obligation with respect to outstanding amounts due to the engineer.

It is not uncommon to see consents with the following wording:

Upon a Default under the Loan Agreement, Engineer, at Lender's request, shall continue performance on Lender's behalf in accordance with the terms of Engineer's Contract, and shall be reimbursed in

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accordance with the Contract for all work, labor, and materials rendered on Lender's behalf subsequent to Lender's request.

Note that the words in bold print will almost certainly not be in bold in the actual consent. What they are saying is that if the lender exercises its rights under the Assignment and requires the engineer to continue performance, the lender has no obligation to pay outstanding amounts due to the engineer. The lender's obligation is limited to compensation for services provided after the lender notifies the engineer that it wants the engineer to continue performance. The engineer would have to file a mechanic's lien against the property for the outstanding amounts. Depending on the priority of its lien, it might receive only a fraction of these amounts, if anything.

The engineer should disagree with these terms and change the provision to read:

...provided that Engineer shall be reimbursed in accordance with the Contract for all work, labor, and materials including all outstanding amounts due.

The lender may object to these terms on the grounds that if it has already advanced

funds to the owner for the engineer's services, it should not have to pay the engineer for those same services. The lender may propose the following as an alternate:

...provided that Engineer shall be reimbursed in accordance with the Contract for all work, labor, and materials including all outstanding amounts due unless Lender has already advanced such funds to the Borrower.

However, the engineer has no control over the lender's disbursements; it is the lender's obligation to monitor the loan.

If the lender does not agree to pay all outstanding amounts due, the engineer should, at a minimum, require the following language:

...including all outstanding amounts due unless Lender had already advanced such funds to the Borrower prior to receipt of Engineer's notice of Borrower's default under Engineer's contract. Lender shall not advance any funds to Borrower for Engineer's services subsequent to receiving such notice.

This puts the burden on the engineer to pay close attention to its payments. If a payment is late and the owner does not provide adequate assurance that the payment will be

made, the engineer should advise the owner that it will notify the lender of the default.

Conclusion

Typically, the request to sign a Consent to Assignment comes when the owner is arranging the construction financing, which may be months after the design agreement was executed. More often than not, it will indicate that the consent needs to be returned immediately because the owner is trying to close on its loan. This can put the engineer in a difficult position if there is objectionable language, particularly if the lender is not willing to negotiate. While the engineer generally has no obligation to sign a consent, refusing to do so can affect its relationship with the owner and jeopardize the prospect of future work. If the owner is already behind on payments to the engineer, it may say that it will not be able to pay until it closes on the loan.

If the lender does not negotiate the terms, the engineer must make a business decision with respect to signing the consent. As a practical matter, unless the project is fast-track, if the owner runs into financial trouble during construction and defaults on its loan,

the engineer will likely have finished the plans and specifications and received payment for them. If the engineer is only doing limited construction administration, it may not have a significant risk with respect to payment. However, unless the consent indemnifies the engineer for the lender or subsequent buyer's use of the plans and specifications, the engineer may still be at risk for claims. ■

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