

# BUDGET BUSTER

## THE FACTS

ABC Engineers provided design services for a residential project. The owner obtained a construction loan from a bank for \$2.7 million; believing he could obtain additional funds from the bank if needed. As construction progressed, they expended the \$2.7 million budget before the project was complete. The bank believed \$2.7 million was adequate to complete the project and denied the owner's request for an additional \$1.3 million. The owner could not obtain additional funds and the contractors stopped working, leaving the project incomplete.<sup>1</sup>

ABC Engineers and various contractors filed suits and liens against the owner for unpaid services and work. This triggered a countersuit as the bank attempted to have the liens cancelled as invalid. The bank also brought a tort claim against ABC Engineers for alleged negligence in certifying the general contractor's pay request with an inaccurate construction cost.

It was felt that ABC Engineers had no liability since they had no duty to the lender. However, things became more complex when the lender went into receivership and was taken over by the FDIC. A trustee was appointed to sort things out. During this process, another bank purchased the 'loan interest' of the bad

loan and claimed it was assigned the right to pursue cost delays and extras against ABC Engineers and the other contractors that filed the fee claims.

## THE RESULT

ABC Engineers' insurance company paid over \$127,000 in indemnity and defense costs even though they were ultimately found not liable.<sup>2</sup>

### RISK FACTOR #1

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Client selection plays an important role in every design firm's risk management program—especially during an economic downturn. Owners/clients in financial distress may look at claims to help get them back on their feet. See our Management Advisory: Professional Practice In An Economic Downturn, for more on this topic.

### RISK FACTOR #2

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Although the insured was ultimately found not liable, their insurance carrier expended over six figures in claims expenses, defense costs, and settlement amounts during the process. This often occurs when design professionals are brought into a lawsuit—even for claims where the design professional is found not liable.

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