MANAGING PROFESSIONAL LIABILITY RISKS IN PREPARING LEGAL OPINIONS

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The rendering of a third-party legal opinion, like other attorney responsibilities in connection with closing a real estate secured finance transaction, involves professional liability risks.[1] This article will discuss how an opinion preparer's use of due diligence and the inclusion in its opinion of customary assumptions, qualifications, limitations, and exclusions (henceforth referred to as assumptions and qualifications) helps to minimize these risks.

As a third-party legal opinion is rendered to a non-client, normally malpractice liability is not involved. Instead, legal opinion claims are normally brought in an action by the opinion recipient based on a theory of negligent misrepresentation. While few lawsuits may be filed annually with respect to legal opinions, notable lawsuits have occurred, and significant judgments or settlements have resulted. Thus, the giving of legal opinions necessitates proper risk management procedures. In determining whether an opinion giver was negligent in preparing a legal opinion, courts often will look to the customary practice related to giving and receiving opinion letters.

The ACREL Attorneys Opinions Committee, along with Legal Opinions in Real Estate Transactions Committee of the American Bar Association Real Property Trusts & Estates Section and the Opinions Committee of the American College of Mortgage Attorneys (collectively, the Real Estate Opinions Committees), have been active over the years in providing guidance regarding customary practice in rendering third-party legal opinions related to real estate finance transactions. Two of the more influential reports issued by the Real Estate Opinions Committees are the Real Estate Finance Opinion Report of 2012 (the 2012 Report)[2] and Local Counsel Opinion Letters in Real Estate Finance Transactions – A Supplement to the Real Estate Finance Opinion Report of 2012 (the Local Counsel Report).[3] The 2012 Report and the Local Counsel Report go into significant detail regarding the due diligence required to render a third-party legal opinion and also discuss customary assumptions and qualifications typically contained in a real estate finance legal opinion. Each report contains an Illustrative Opinion setting forth model language to address both due diligence and forms of assumptions and qualifications.

Firm Policies

Law firms seeking to minimize their professional liability risks related to opinions may establish policies and procedures related to their attorneys who issue opinion letters. Last fall the American Bar Association Business Law Section Legal Opinions

Committee issued its Report on 2019 Survey of Law Firm Opinion Practices[4] (the Report). The Report reflects the results of a survey of approximately 300 law firms throughout the United States regarding the policies and procedures law firms maintain with respect to their third-party legal opinion practice. As noted in the introduction to the Report:

> Most law firms have policies and procedures for the preparation and delivery of legal opinion letters to recipients who are not their clients. The policies typically identify the opinions a firm is willing and unwilling to give, and the procedures establish the steps opinion preparers are expected or encouraged to take before they deliver an opinion letter on behalf of the firm. Firms often provide their lawyers with sample opinion letters and assign various responsibilities for the opinion letters their firm delivers to a committee or committees of the firm's lawyers (an "opinion committee").[5]

The Report also contains a discussion of selected areas of law that may or may not be covered in opinions given by various law firms in the country, including Delaware law opinions by non-Delaware lawyers, laws of other states besides Delaware where the opining lawyer is not admitted, UCC opinions, no-litigation confirmations, no breach or default opinions, and the enforceability of arbitration clauses.

While strong firm policies and procedures can help reduce the professional liability risks in rendering third-party legal opinions, the actual wording of the legal opinions and the due diligence performed in preparing the legal opinions are essential parts of professional liability risk management.

Customary Practice

Over the years, various bar associations, committees, and others have tried to develop guidance and protocols with respect to rendering legal opinions. This has evolved into what is referred to as customary practice. Under customary practice, the meaning of the words used in an opinion letter, and the diligence required to provide such an opinion letter, are determined by the customary practice of lawyers who regularly give and receive such opinion letters. The Real Estate Opinion Guidelines[6] provide valuable guidance regarding customary real estate opinion letter practice.[7] As customary practice may vary due to regional or practice-related differences, it is not always possible to precisely identify what is customary practice. Reports by bar groups and opinion committees are helpful in identifying customary practice in certain areas. Also, the Customary Practice Statement,[8] which has been adopted by numerous bar associations and groups, including the Real Estate Opinion Committees, summarizes opinion letter customary practice.[9]

A main reason for the focus on customary practice is to enable opinion givers and opinion recipients to understand the generally accepted meaning of words normally used in legal opinions and what due diligence is needed in order to render specific legal opinions. Since the words in a legal opinion can create risks to the opinion giver, and the failure to perform adequate due diligence can also create risks, the various opinion reports have extensive discussions of what is meant by customary practice, what the words used in a legal opinion mean, and what due diligence is required to satisfy the customary practice standards of lawyers rendering opinions.

Due Diligence

Because legal opinions require the review of facts, documents, and the law, one important way an opinion giver may limit professional liability in an opinion letter is to specify the due diligence done in connection with the preparation of the legal opinion. Customary practice provides an opinion giver will have completed such due diligence as is customarily required in order to render a legal opinion. This normally includes reviewing the underlying transaction documents, the organizational documents related to the opinion giver's client that is the subject of the opinion, and public authority documents. It is customary to describe in detail each of the various transaction documents, client documents, and authority documents reviewed by

the opinion giver. When certain facts cannot easily be confirmed in due diligence, opinion letters often rely on certificates of the client and other interested parties to establish certain factual (but not legal) matters. Finally, an opinion giver may state what laws it has considered and what laws are the subject of the opinion. Normally these are laws of the jurisdiction where the opinion giver is opining and, at times, federal law (except in the case of local counsel opinions).[10] When the opinion giver is acting as local or special counsel, the opinion giver may also wish to state this in its opinion letter to show that it has a limited role in the transaction.

As noted in the 2012 Report, "opinion letters often include statements to the effect that, in addition to identified documents, the opinion giver has reviewed such matters as are necessary in the professional judgment of the opinion giver to render the opinion. Customary practice dictates that the opinion giver has undertaken review of what is necessary to render the opinion letter; therefore such a statement is unnecessary in the opinion letter."[11] Nevertheless, an opinion giver often will limit the scope of inquiries to specific documents or specific items, but also as noted in the 2012 Report, "such a limitation is effective only if it is explicit."[12] "Recitation of a list of documents without an express limitation in the scope of the review should not be relied upon as being effective to limit the scope of review."[13]

As a general matter, an opinion giver can rely on client certificates and public authority and other documents with respect to the factual information contained therein without any additional investigation, unless the opinion giver has actual knowledge that the information is false or misleading or if he does not believe the source is appropriate. As stated in the Business Opinion Guidelines (also as included in the Real Estate Opinion Guidelines), "An opinion giver should not render an opinion that the opinion giver recognizes will mislead the recipient with regard to matters addressed by the opinions given."[14]

When dealing with multi-tiered entities (e.g., a limited liability company borrower with a limited liability company manager that itself is owned by various entities), the issue arises whether as part of due diligence an opinion giver must examine the entity or entities for each level and go "up the chain" to verify that all necessary approvals and consents have been taken. The TriBar Opinion Committee takes the position that this is unnecessary and that it is implicitly assumed that all up the chain approvals have been given unless such an implicit assumption would be unreasonable under the circumstances.[15] The 2012 Report and the Local Counsel Report state that opinion givers should consider an express assumption as to these approvals to avoid having to rely on an implicit assumption.[16]

Assumptions and Qualifications

Another important area of risk management includes the inclusion in third-party legal opinions of express (or implicit) assumptions and qualifications, many of which are commonly accepted, and many of which are also implied as a matter of customary practice.

If one were to render a legal opinion without normal assumptions and qualifications, the opinion would be relatively short like the following example:

> The Borrower has done everything it needs to do to authorize the execution and delivery of the loan documents, the authorization, execution and delivery and performance of loan documents will not violate anything, and each and every provision of the loan documents will be enforceable as written.

No lawyer experienced in rendering legal opinions would render such an opinion. Similarly, no lawyer experienced in receiving legal opinions would accept or rely upon such a legal opinion as it clearly indicates the opinion giver is not familiar with the customary practice of rendering legal opinions. This would be tantamount to accepting the anecdotal legal opinion where the opinion giver simply pastes the lender's proposed form of legal opinion on its letterhead, signs it, and returns it to the lender. Customary practice also dictates that both opinion givers and opinion recipients understand

customary practice as it relates to the meaning of an opinion.

Why are assumptions and qualifications customarily included in third-party legal opinions? The answer is because without such assumptions and qualifications, an opinion giver would be rendering an opinion similar to the sample short form opinion set forth above. There would be no limitations or qualifications concerning the documents the opinion giver reviewed, what due diligence was done, and if there are any exceptions, limitations, or exclusions with respect to the breadth of the enforceability opinion contained in a standard third-party real estate finance opinion.

The enforceability opinion is the substantive legal opinion most affected by assumptions and qualifications. The typical enforceability opinion provides that a court would grant a remedy for the breach of a covenant in the agreement that is the subject of the enforceability opinion. However, it is widely known that detailed loan agreements and real estate mortgages or deeds of trust often include provisions of questionable validity, and remedies that may be available only under certain circumstances. Without the insertion of qualifications, an enforceability opinion could be interpreted to provide that each and every provision of a loan document is enforceable as written, and every remedy would be given effect as provided in the loan documents. This is what was frequently referred to as the New York approach to enforceability. This is in contrast to the California approach under which only the material provisions in the loan documents would be enforceable and the material remedies provided would be available only after a material default. Over the decades, as customary practice has evolved, which includes the insertion of qualifications in the opinion, the distinction between the California and the New York approaches has become irrelevant.

The 2012 Report, in its Illustrative Opinion, lists assumptions commonly included within real estate finance opinions, and provides that customary practice implies these assumptions whether or not they are expressly stated:[17]

(a) A Borrower or Guarantor who is a natural person, and natural persons who are involved on behalf of either of the Borrower or the Guarantor, have sufficient legal capacity to enter into and perform the Transaction or to carry out their role in it.

(b) The Borrower holds the requisite title and rights in and to any property involved in the Transaction.

(c) Each party to the Transaction (other than the Borrower and the Guarantor) has satisfied those legal requirements that are applicable to it to the extent necessary to make the Transaction Documents enforceable against it, and each such party's obligations set forth therein are enforceable against it in accordance with all stated terms.

(d) Each party to the Transaction (other than the Borrower and the Guarantor) has complied with all legal requirements pertaining to its status as such status relates to its rights to enforce the Transaction Documents against the Borrower and the Guarantor.

(e) Each Transaction Document, Authority Document, and other document submitted to us for review is accurate and complete, each such document that is an original is authentic, each such document that is a copy conforms to an authentic original, and all signatures on each such document are genuine. The form and content of all Transaction Documents submitted to us as unexecuted drafts do not differ in any respect relevant to this Opinion Letter from the form and content of such Transaction Documents as executed and delivered.

(f) Each Public Authority Document is accurate, complete, and authentic, and all official public records (including their due and proper recordation or filing, and their due and proper indexing) are accurate and complete.

(g) The Security Documents have been or will be duly and properly recorded or filed and duly and properly indexed in all places necessary (if and to the extent necessary) to create the encumbrance and lien as provided therein.

(h) The description of the Collateral is accurate and reasonably identifies the Collateral.

(i) Legally adequate consideration has been given for the Transaction and the obligations of the Borrower and the Guarantor in the Transaction Documents.[18]

Another six assumptions that are often also included in real estate finance opinions and also implied by customary practice[19] are also listed in the 2012 Report:

(j) There has not been any mutual mistake of fact or misunderstanding, fraud, duress, or undue influence.

(k) The conduct of the parties to the Transaction has complied and will continue to comply with any requirement of good faith, fair dealing, and conscionability.

(l) The Lender and any agent acting for the Lender in connection with the Transaction have acted in good faith and without notice of any defense against the enforcement of any rights created by the Transaction, or of any adverse claim to any property, lien, or securing interest transferred, or created as part of the Transaction, or of any agreement, or court or administrative order, writ, judgment, or decree that would be violated by entering into the Transaction, or by execution, delivery, or performance of the Transaction Documents.

(m) There are no agreements or understandings among the parties, written or oral, and there is no usage of trade or course of prior dealing among the parties that would, in either case, define, supplement, or qualify the terms of the Transaction Documents.

(n) All statutes, judicial and administrative decisions, and rules and regulations of governmental agencies, constituting the Law of the Opinion Jurisdictions are generally available (i.e., in terms of access and distribution following publication or other release) to lawyers practicing in the Opinion Jurisdictions, and are in a format that makes legal research reasonably feasible.

(o) The constitutionality or validity of a relevant statute, rule, regulation, or agency action is not in issue unless a reported decision in the Opinion Jurisdictions has specifically addressed but not resolved, or has established, its unconstitutionality or invalidity.[20]

In addition, the 2012 Report provides for the insertion of other assumptions appropriate for other state, entity, or transaction-specific assumptions, such as choice of law.

Local Counsel Opinions

In addition, local counsel opinions present risks for an opinion giver since normally local counsel have little, if any, direct contact with the borrower client. Often times, the local counsel is retained by lead counsel who has the sole direct contact with the client, and a local counsel's knowledge of matters with respect to the borrower is extremely limited. Typically, local counsel will only review certain documents that are relevant to the local jurisdiction, including security documents and organizational documents if the borrower or guarantor are organized in the opinion giver's jurisdiction. One way to establish this limited role in the transaction is for the opinion giver to expressly state its role as local counsel in the introduction to the opinion.

Additional common assumptions set forth in the Local Counsel Supplement deal with local counsel issues and with respect to entity and guarantor assumptions. The Local Counsel Report Illustrative Opinion also has two assumptions that are important to note. One deals with the up-the-chain-approvals issue previously discussed and provides as follows:

(q) Each of the persons whose consent is required to authorize the Borrower or the Guarantor to execute and deliver the Transaction Documents and perform its agreements thereunder, if an entity, (i) is validly existing and in good standing under the Law of the jurisdiction of its organization or formation and (ii) has taken all action necessary under any applicable organizational documents and applicable Law to authorize the execution and delivery of the Transaction Documents to which the Borrower or the Guarantor is a party and the performance of the Borrower's or the Guarantor's obligations thereunder.[21]

The second concerns the type of entity involved in the transaction and assumes the entity is not subject to any special governmental restrictions on its activities—facts that are seldom known by local counsel. This assumption reads:

(w) The Borrower [or the Guarantor] is a general business entity of a type that is not regulated by governmental authority or court order in a way that would restrict the ability of the Borrower [or the Guarantor] to alienate or encumber its property to secure indebtedness [or to enter into the Transaction Documents].[22]

Qualifications, Limitations, and Exclusions

In addition to listing common assumptions, opinion letters typically also contain customary qualifications, exceptions, and limitations (referred to hereinafter as qualifications).

Two qualifications that are understood by customary practice to be implied in an opinion, whether or not stated, are the bankruptcy exception and the equitable principles exception.[23] The bankruptcy exception is not limited to matters under the federal Bankruptcy Code. The bankruptcy exception also covers all federal and state bankruptcy, insolvency, reorganization, receivership, moratorium, and similar laws that may affect the rights and remedies of creditors generally. Also, the bankruptcy exception applies to all of the substantive opinions, and not just to the enforceability opinion.[24]

The equitable-principles exception covers a host of equity-based limitations that might affect a creditor's right to enforce its remedies. Some opinion givers may just use a short generic qualification to "equitable principles" while others may include a more expansive list such as the list set forth in the 2012 Report Illustrative Opinion.[25]

An important concern to opinion givers in rendering an enforceability opinion are the various provisions in a loan document that may not be enforceable as written and that are not otherwise covered by the bankruptcy or equitable principles qualifications. As noted earlier, lawyers usually recognize that commercial real estate loan transactions include numerous provisions of doubtful or questionable validity as they might depend on certain facts or the law in existence at the time remedies may be sought or might otherwise violate applicable law or public policy. There are two principal ways to deal with this issue. Historically, real estate finance opinion givers would include language that would take a broad generic exception to the effect that while certain provisions and remedies set forth in loan documents might not be enforceable, their inclusion does not affect the validity of the documents as a whole or the practical realization of the substantive benefits that are intended to be provided by the loan documents.

The use of the "practical realization" generic qualification has been criticized by many in the real estate finance area (and others), as being too vague and unspecific. In order to provide more specificity with respect to what may be covered in a legal opinion, the Real Estate Opinions Committees adopted what is referred to as the Generic Qualification with Assurance. The 2012 Report has this form of generic qualification and assurance:

4.3 Generic Enforceability Qualification[, with Assurance]: Certain provisions of the Transaction Documents may not be enforceable; nevertheless, subject to the other limitations set forth in this Opinion Letter, any such unenforceability will not render the Transaction Documents invalid as a whole or preclude

(i) the judicial enforcement in accordance with applicable Law of the obligation of the Borrower to repay as provided in the Note the principal, together with interest thereon (to the extent not deemed a penalty), and the judicial enforcement in accordance with applicable Law of the obligation of the Guarantor to repay as provided in the Guaranty the amounts set forth in the Guaranty (to the extent not deemed a penalty and subject to defenses of a surety that have not been or cannot be waived); (ii) the acceleration of the obligation of the Borrower to repay such principal, together with such interest, upon a material default by the Borrower in the payment of such principal or interest [or upon a material default by the Borrower in any other material provision of the Transaction Documents]; and (iii) the foreclosure in accordance with applicable Law of the lien on and security interest in the Collateral created by the Security Documents upon maturity or upon acceleration pursuant to clause (ii) above.[26]

In addition to the bankruptcy, equitable principles, and general qualifications, opinion givers may wish to include certain transaction-related qualifications such as unique matters of state law that are significant or material.[27] As noted in the 2012 Report, in addition to the bankruptcy, equitable principles, generic, and other transaction-related qualifications, opinion letters may list other general qualifications that normally refer to remedies.[28] Others prefer not to use this "laundry list" approach since properly drafted bankruptcy, equitable principles, generic, and transaction-related qualifications should suffice.[29]

Exclusions

The 2012 Report lists a number of common exclusions that are included in opinions. These exclusions relate to areas of law that are not routinely covered by a typical real estate finance opinion. A recent article, Laws Commonly Excluded from the Coverage of Third-Party Legal Opinions in U.S. Commercial Loan Transactions,[30] discusses these commonly excluded laws and why they are either implicitly considered not to apply to a legal opinion, or as is often the case, specifically excluded in the opinion.

The article identifies the following laws as excluded by customary practice even when they are recognized as applicable to the transaction:

- Laws of jurisdictions not expressly stated in the covering opinion letter;
- Municipal and other local laws;
- Securities laws;
- Tax laws;
- Insolvency laws;
- Anti-trust laws; and
- Fiduciary duty requirements.[31]

The laws that are rarely, if ever, addressed in the loan context were listed as follows:

- Anti-fraud laws;
- Laws addressing privacy matters;
- Laws addressing immigration and naturalization;
- Laws addressing occupational, safety and health, or other similar matters;
- Laws addressing labor, pension, or other employee rights and benefits;
- Laws addressing corrupt practices;
- Laws addressing racketeering, criminal or civil forfeiture, or other criminal acts (including mail and wire fraud);
- Laws addressing zoning, land use, subdivisions, building, or construction matters;
- The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, and laws applicable to swaps and other derivatives, commodity (and other) futures and indices, and other similar instruments;
- Laws addressing foreign asset or trading controls, emergencies, national security, terrorism, or money laundering;

- Laws addressing other aspects of foreign investment, including Section 721 of the Defense Production Act of 1950, as amended and the related regulations overseen by the Committee on Foreign Investment in the United States (CFIUS); and
- Possible judicial deference to acts of sovereign states (including judicial action given effect to governmental actions or foreign laws affecting predator's rights).[32]

In a final grouping, the article cites examples of what the authors considered commonly excluded laws that are sometimes expressly covered when both applicable and significant to the transaction entity. The examples listed are:

- Environmental laws;
- The Hague Securities Convention;
- Laws relating to security interests in specialized forms of collateral (e.g., patents, trademarks, trade secrets, and registered copyrights), vessels documented under the laws of the United States, aircraft (and certain related aircraft parts and equipment), rail cars, locomotives and rolling stock; and
- Laws applicable to regulated industries (e.g., public utilities, telecommunications, banking, or insurance).[33]

Should You Rely on Implicit Assumptions and Qualifications or Expressly State Them?

As noted earlier, certain of the commonly accepted assumptions and qualifications are considered as a matter of customary practice to be implied in a legal opinion even if not stated. The TriBar Opinions Committee takes the position that commonly used assumptions and qualifications are implicit and need not be specifically stated.[34] This reflects the TriBar's preference for short, streamlined legal opinions. This differs from the normal real estate finance approach which uses detailed opinions listing specific assumptions and qualifications.

Should an opinion giver rely just on customary practice or include explicit assumptions and qualifications? The 2012 Report discusses this as follows:

> More recently, the Customary Practice Statement[35] notes that customary opinion letter practice provides content to abbreviated opinion letter language, thus allowing shorter forms of opinion letters. The Customary Practice Statement, however, does not require short opinion letters. The questions remain: How short is too short? And, how much precision in language is necessary to convey the meanings of the words used in an opinion letter? These questions pertain particularly to stated assumptions and limitations. As is noted in further discussion in Chapter Two, many assumptions and limitations can be implied through customary practice. Nevertheless, until customary practice that has established accepted and essential normative conduct in opinion practice has become so ingrained and judicially accepted that no arguable doubt can be cast on the effect of omission of an assumption or limitation, or unspoken limitation of diligence required to render an opinion, there is risk inherent – at least procedurally – in relying on customary practice to "fill in the blanks."
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> Real estate finance lawyers tend to use lengthier opinion letters than are used by many of their counterparts in other business transactions. This may result in part from the nature of the type of transaction, but it also may result in part from viewing matters through a different lens than other business lawyers, and from the nuanced legal issues that attend a sophisticated real estate secured financing transaction.
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> Conversely, while supporting the use of somewhat longer opinion letters, the Committees recognize the opposite danger: that a lengthy opinion letter might give false comfort that it is completely comprehensive. As noted in the Customary Practice Statement, while an opinion letter might on the surface seem to be comprehensive, an opinion letter

> cannot express all of the gloss that customary practice will add to understanding an opinion letter.[36]

While there are benefits to both the TriBar and real estate approaches, there is a professional liability risk issue to be considered depending on which path is chosen. If one were to follow the TriBar approach and rely on a shortened form of legal opinion on the basis that customary practice implies many provisions that are inherent in legal opinions, and the matter later results in a dispute, it would be necessary to introduce expert testimony in any resulting legal proceeding as to whether customary practice was followed and whether a shortened form legal opinion has certain assumptions and qualifications that are, as a matter of customary practice, implied even if not stated. On the other hand, the more detailed real estate approach includes specific language that would eliminate any argument whether or not a stated assumption and qualification is included in the opinion as it would be expressly set forth in the opinion.

Two cases, *Fortress Credit Corp. v. Dechert LLP*[37] and *In re SonicBlue, Inc.*[38] help to demonstrate the different approaches and how customary practice and a short form versus long form of opinion may make a difference from a liability standpoint.

Fortress involved a fraudulent scheme where the Dechert firm was contacted by attorney Marc Dreier (who later went to prison for his felonious actions) to render an opinion for a borrower in connection with a loan from Fortress Credit Corp. The borrower was an entity represented by Dreier, and Dreier himself was a guarantor of the loan. In reality Dreier's purported client had no knowledge of the transaction and Dreier stole all the funds. Dreier forged the signatures of his purported client on all loan documents (as well as the engagement letter with Dechert). When the scheme unraveled, the lender sued Dechert under various causes of liability as Dechert had rendered a legal opinion stating the loan documents were valid and enforceable against the unwitting and unknowing borrower. The case took several years to be resolved, and ultimately Dechert prevailed on appeal. The appellate court found that Dechert's legal opinion: (i) was limited by express assumptions as to the genuineness of signatures and the authenticity of documents; and (ii) included a disclaimer that the firm had not undertaken any independent inquiry or investigation beyond a review of the loan documents. While the assumptions of the genuineness of signatures and the authenticity of documents relied upon by an opinion giver are by customary practice implicit in an opinion, whether expressed or not, the *Dechert* court held that by including these express assumptions and limitations, the Dechert firm had no liability. Thus, *Dechert* supports the proposition that setting forth express assumptions and qualifications in a legal opinion limits professional liability risk making it unnecessary to introduce evidence of customary practice that the relevant assumptions and limitations are implied even if they are not expressly stated.

SonicBlue illustrates not only the perils of faulty opinion drafting, but also how customary practice may have prevented a negligent misrepresentation claim because of language omitted from the opinion. In *SonicBlue*, a legal opinion was delivered covering certain transactions in a bond deal. Due to what was perceived as a "scrivener's error," the bankruptcy and equitable principles limitations were inserted to only apply to one, but not both, of two separate enforceability opinions set forth in the opinion letter. Here are the relevant opinion excerpts:

> 2. . . . [T]he Purchase Agreement, the Registration Rights Agreement, the Indenture, the Pledge and Security Agreement and the Option Agreement, when duly executed and delivered by the Buyers, will each constitute a valid and binding agreement of the Company, enforceable against the Company in accordance with its terms.
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> * * *
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> 3. The issuance and sale of the Debentures have been duly authorized. Upon issuance and delivery against payment therefor in

> accordance with the terms of the Indenture and the Purchase Agreement, the Debentures will constitute valid and binding obligations of the Company, enforceable against the Company in accordance with their terms.
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> * * *
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> 9 . . . (b) Our opinion in paragraph 2 above is subject to and limited by (i) the effect of applicable bankruptcy, insolvency, reorganization, fraudulent conveyance, receivership, conservatorship, arrangement, moratorium or other laws affecting or relating to the rights of creditors generally . . .

The law firm that rendered the opinion letter was representing the debtor when it became bankrupt and sought to remain as counsel to the debtor in the bankruptcy proceedings. This resulted in a conflict of interest in the bankruptcy case because of the work the law firm had performed for the debtor and because of the inaccurate legal opinion where the bankruptcy exception did not specifically apply to both of these substantive enforceability provisions. The case was ultimately settled, so the court never ruled on whether or not the bankruptcy exception that was omitted from one of two substantive provisions should have been implied as a matter of customary practice. Nevertheless, *SonicBlue* illustrates the need to make all assumptions and qualifications apply to all of the substantive opinions and not to just certain specific provisions.

Reliance

Reliance is another area of professional liability concern to opinion givers because the range of persons who may be entitled to rely, and ultimately sue, on a legal opinion should be narrowed as much as possible. It is customary to provide that the original lender can rely on the legal opinion. Some opinion recipients request broad reliance language that will allow the lender's successors and assigns to be able to rely on the opinion, as well as the lender's attorneys, accountants, and rating agencies.[39] In addition, loan participants and parties to a syndicated transaction sometimes may request reliance on the opinion. A broader list of parties that may rely on the opinion exposes the opinion giver to greater liability. Thus, an opinion giver should seek to narrow who may rely on an opinion. Also, it is important to limit the timeframe for which a party is entitled to rely on the opinion. As a general rule reflected in customary practice, an opinion speaks for itself only on the date it is issued. However, some fear that when an assignee or transferee of a loan acquires a loan, that the opinion may be deemed re-issued or that the reliance may start from that date. To help address these concerns, what is commonly known as the Wachovia type of reliance evolved that specifically limits who may rely on an opinion and that the opinion may only be relied on as of the date of the opinion. The Local Counsel Report includes an example of a tailored reliance clause that is as follows:

> 5.1 Use. The opinions expressed in this Opinion Letter are solely for the [Lender's] [addressee's] use in connection with the Transaction for the purposes contemplated by the Transaction Documents. Without our prior written consent, this Opinion Letter may not be used or relied upon by the [Lender] [addressee] for any other purpose whatsoever or relied on by any other person[, except that this Opinion Letter may be delivered by the [Lender] [addressee] to an assignee from time to time for value in good faith of all right, title, and interest in and to the [Note] [Transaction Documents], and such assignee may rely on this Opinion Letter as if it were addressed and had been delivered to it on the date hereof]. Nothing in the preceding sentences, however, shall give any person entitled to rely upon this Opinion Letter any greater rights with respect to this Opinion Letter than those of the [Lender] [addressee] as of the date hereof, or shall provide or imply any opinion being given with respect to an assignee that depends on the identity or characteristics of the named assignee or circumstances other than those at the date of this Opinion Letter. This Opinion Letter may be delivered (i) to a regulatory agency having supervisory authority over the [Lender] [addressee] for the purpose

of confirming the existence of this Opinion Letter; (ii) to the court or arbitrator and parties to a litigation or arbitration in connection with the assertion of a defense as to which this Opinion Letter is relevant and necessary; (iii) to nationally recognized statistical rating organizations rating an issuance involving [the Loan] or otherwise entitled to access under Rule 17g-5 under the Securities and Exchange Act of 1934, as amended (or any successor provision to such subsection) by providing a copy of this Opinion Letter to the appropriate 17g-5 information provider for the securitization into which the Loan or a component of the Loan is deposited or as otherwise permitted by the applicable pooling and servicing agreement or trust and servicing agreement, as the case may be; and (iv) to other parties as required by the order of a court of competent jurisdiction in the United States.[40]

The Local Counsel Report further suggests including the following provision that authorizes but limits reliance by assignees of a lender:

> The opinions expressed in this Opinion Letter are solely for the benefit of the addressee[s]. We consent to reliance on the opinions expressed in this Opinion Letter, solely in connection with the Opinion Transaction Documents, by any assignee of the Lender's interest subsequent to the date of this Opinion Letter (each an "Assignee") as if this Opinion Letter were addressed and delivered to such Assignee on the date of this Opinion Letter, on the condition and understanding that (i) any such reliance must be actual and reasonable under the circum-stances existing at the time such Assignee becomes a Lender, including any circumstances relating to changes in Law, facts, or any other developments known to or reasonably knowable by such Assignee at such time, (ii) our consent to such reliance shall not constitute a reissuance of the opinions expressed in this Opinion Letter or otherwise extend any statute of limitations period applicable hereto on the date hereof, and (iii) in no event shall any Assignee have any greater rights with respect hereto than the original addressee[s] of this Opinion Letter on its date.[41]

Knowledge

In the past, opinion givers were frequently asked to render opinions based on the opinion giver's knowledge of certain facts (e.g. the existence of litigation that might affect the borrower, the transaction, or the collateral, if the borrower was in default under its obligations, or if the loan transaction might cause a default under other agreements). These are not opinions but are facts. Over time, the practice has evolved and many attorneys now decline to provide such facts on the basis that a lender and its counsel can get comfortable about these factual matters through search reports and representations and warranties made by the borrower in the loan documents.[42]

When confirmations are provided, it is best to identify and narrow whose knowledge applies (e.g. the opinion drafter, the deal team, or the entire firm) and to limit knowledge to the "conscious awareness" of facts without investigation or inquiry.[43] Also, as local counsel seldom have any direct dealings with, or knowledge about, the client, it is more appropriate for lead counsel to render any such opinions as to knowledge.[44] Another way to avoid the "knowledge" risk is for the opinion giver to describe each document or other matter that its opinion covers rather than referring to actions or documents known to the opinion giver.

Notes

1 A prior version of this article was published in The ACREL Papers – Oct. 2023.

2 47 Real Prop. Tr. & Est. L. J. 213 (2012).

3 51 Real Prop. Tr. & Est. L.J. 167 (2016).

4 77 Bus. Law 1163 (2022).

5 Id. (citations omitted).

6 ACREL Attorneys' Opinion Committee and ABA Section of Real Property, Probate and Trust Law Committee on Legal Opinions in Real Estate Transactions, Real Estate Opinion Letter Guidelines, 38 Real Prop. Prob. & Tr. J. 241 (2003) [hereinafter Real Estate Opinion Guidelines]. The Real Estate Opinion Guidelines refer to and adapt, for real estate opinion letters, the Committee on Legal Opinions of the Section of Business Law of the ABA, Guidelines for the Preparation of Closing Opinions, 57 Bus. Law. 875 (2002) [hereinafter Business Opinion Guidelines].

7 2012 Report, supra note 2, at 220, n. 1.

8 Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions, 63 Bus. Law. 1277 (2008) (the Customary Practice Statement).

9 2012 Report, supra note 2, at 220-1.

10 2012 Report, supra note 2, at 185-86.

11 Id. at 231.

12 Id.

13 Id.

14 Id. at 233.

15 TriBar Opinion Committee, Third-Party Closing Opinions: Limited Liability Companies, 61 Bus. Law. 679, 689 n. 52 (2006).

16 See 2012 Report, supra note 2, at 239; Local Counsel Report, supra note 3, at 195.

17 Id. at 234.

18 Id. at 263-4.

19 Id. at 265.

20 Id.

21 Local Counsel Report, supra note 3, at 248.

22 Id. at 249-50.

23 2012 Report, supra note 2, at 251-52.

24 Id.

25 Id. at 251-52, 268.

26 Id. at 268-69.

27 Id. at 255.

28 Id.; see example of other general qualifications at 269-70.

29 Id.

30 Merel, Gail (Reporter), Adcock, A. Mark, Barron, Robert W., Buck, Jr., Willis R., Grossman, Jerome A., Hering, Louis G., Hoxie, Timothy G., Kaufman, Andrew M., Ryan, Jr., Reade H., Schwartz, Philip B., and Tarry, Stephen C. 76 Bus. Law. 889 (2021).

31 Id. at 894-96.

32 Id. 899-900

33 Id. at 909-912.

34 Special Report of the TriBar Opinion Committee: The Remedies Opinion – Deciding When to Include Exceptions and Assumptions. 59 Bus. Law. 1449 (2004).

35 Supra note 8.

36 2012 Report, supra note 2, at 222-3.

37 Fortress Credit Corp. v. Dechert LLP, 934 N.Y.S. 2d 119 (App. Div. 2011).

38 In re SonicBlue Incorporated, 2008 WL 170562 (Bankr. N.D. Cal 2008).

39 See Local Counsel Report, supra note 3, at 234-5 for a discussion that rating agencies only need to be provided with a copy of the opinion and have no need to rely upon it.

40 Id. at 263.

41 Id. at 264.

42 2012 Report, supra note 2, at 257.

43 Id.

44 Local Counsel Report, supra note 3, at 234.