

"Toward an Emerging Consensus in Real Legal Opinion Practice"¹

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A. Customary Practice

1. Three generations of real estate opinion letter commentary.
 - (a) Pre-Accord state bar reports, including the 1987 California Real Estate report, the 1989 New York Mortgage Loan Report and the 1989 Maryland Bar Report.
 - (b) The 1991 ABA Business Law Accord Report and its progeny, including the ABA/ACREL Accord Adaptation Report, the ABA/ACREL Inclusive Opinion, and various state bar Accord-based reports.
 - (c) "Customary practice", including the ABA Business Law Opinion Guidelines, the TriBar Closing Opinion Report, the ABA/ACREL Real Estate Opinion Guidelines, additional state bar real estate reports, including the 1998 New York Mortgage Loan Opinion Report and 2007 Maryland Bar report.
2. The "Customary Practice" approach was first taken up by the Business Law Section and Tri Bar committees after the perceived failure of the acceptance of the Accord as an opinion protocol.
3. Comparison of Customary Practice with other approaches.
 - (a) The traditional model, prior to the Accord, was a fully articulated opinion that attempts to set forth all of the definitions, qualifications and other terms of the opinion within the "four corners" of the document itself, generating famously lengthy opinion letters and, in the view of some, taking a "kitchen sink" approach.
 - (b) The Accord is a protocol designed to be adopted by the parties as a definitional gloss on a very brief opinion letter; it can be viewed as a contractual arrangement supplementing a short form opinion. Several state bar opinion reports (e.g., California, Texas, etc.) have recommended

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the same approach, adding conventions relating to local law issues and practices.

- (c) The more recent "Customary Practice" approach, as with the Accord, recommends a "streamlined" form of opinion, the interpretation of which is supplied by a body of customary understanding and practice gleaned from the state bar opinion reports and other commentary and opinions, as well as the accepted local usage employed by opinion parties.
- (d) Advantages and Disadvantages of Customary Practice.
- (e) Arguments for Customary Practice:
 - (i) Allows for more concise and readable opinion letter.
 - (ii) Makes it easy to identify purported changes from the standard.
 - (iii) Recognizes the importance of extrinsic understandings and conventions; avoids literal, unqualified interpretations by a reviewing court of opinion letter intent.
 - (iv) Articulates and incorporates the common sense assumptions of the opinion parties as to how opinions will be understood and interpreted.
- (f) Arguments Against Customary Practice:
 - (i) Customary practice is locally defined and may differ in different legal communities.
 - (ii) Whose Customary Practice governs in the case of interjurisdictional opinion letters?
 - (iii) Customary practice may not be well defined or may be ambiguous; an elaborate fully articulated opinion provides more assurance against miscommunication, misunderstanding and unintended liability.

B. The Enforceability or Remedies Opinion.

1. Is an enforceability opinion necessary or appropriate where both lawyers practice in the same jurisdiction?
 - (a) Justifications often given for a third party opinion are that it:
 - (i) Provides assurances regarding enforceability.
 - (ii) Establishes good faith meeting of the minds.

- (iii) Makes it more difficult and may create an estoppel against raising defenses to enforcement.
 - (iv) Assures that Borrower's lawyer is giving same advice to lender as to client.
 - (b) Rebuttals include that:
 - (i) The lender's counsel has an independent professional responsibility to advise clients of problematic provisions and issues. Arguably third party opinion are not even actionable, given the absence of reasonable reliance.
 - (ii) An opinion reflects a meeting of the lawyers' minds, not necessarily those of the clients; anything further is an unrealistic imputation of intent.
 - (iii) A lawyer may effectively be estopped, but not the client.
 - (iv) It is unlikely that a lawyer will discuss the content of an opinion with the client. In the unusual case that the opinion covers the adequacy of documents, revealing client secrets or communications raises ethical issues; unless client consents to disclosure, the lawyer may have to withdraw.
 - (v) It adds cost and inefficiency to the transaction.
2. Scope of standard opinion letter language.
- (a) The words "legal," "valid," "binding," "enforceable," "enforceable in accordance with its terms" each previously connoted different aspects of an enforceability opinion. Now the key phrase is simply "enforceable."
 - (b) The *prima facie* meaning of enforceable differs—New York (each and every provision) vs. California (all essential or material provisions).
3. Assuming that the "each and every" meaning may be operative, the issue becomes how to identify recognized exceptions to enforceability.
- (a) Bankruptcy exception.
 - (i) This is an expansive concept included in the real estate reports; it includes fraudulent conveyances, inadequate consideration, etc.
 - (ii) Note special concerns regarding mortgages and deeds of trust by third parties; which constitute upstream or sidestream guaranties.
 - (b) Equitable principles exception.

- (i) Again, the real estate reports support broad coverage, including waiver, laches, estoppel and other equitable defenses, as well as specific performance, injunction and other equitable remedies.
 - (ii) Typical real estate concerns relate to foreclosure, assignment of rents, other pre-foreclosure remedies.
- (c) Other exceptions to enforceability:
- (i) The "laundry list" identifies limitations on enforcement of various remedies, covenants or other loan provisions.
 - (ii) The "generic exception" alternative sets forth a generalized exception that some or more provisions of loan documents may not be legally enforceable, but that the lender will nonetheless be afforded certain fundamental rights of enforcement. This "comfort language" takes various forms:
 - (A) "Practical realization of principal benefits."
 - (a) This is the traditional statement in early real estate opinion practice (and is still used in specialized financings and some other non-real estate contexts).
 - (b) Because of the ambiguities inherent in this language regarding which stated remedies constitute "practical realization" and which rights and covenants constitute "principal benefits," this version is increasingly disfavored.
 - (B) Acceleration and payment and/or foreclosure in the event of "material breach of a material covenant."
 - (a) Because of the clarity of the assured remedy (payment and/or foreclosure) and the judicially recognized concept of materiality, this is an increasingly favored approach.
 - (b) Note that the acceptability of the "material breach" exception may be the result of the easy identification of the lender's primary concern; i.e., acceleration of the debt and payment or foreclosure.
 - (c) Moreover, this language is not without its own ambiguities; i.e., is the meaning of "material breach" really that clear?

- (iii) The "hybrid approach" (a generic exception with relatively short laundry list) may be, in practice, the most widely used method.

C. Specific Issues Regarding Enforceability

1. Usury.
 - (a) The non-violation of applicable usury laws is generally deemed implied by a general enforceability opinion, but the subject is usually expressly addressed.
 - (b) This is rarely a problem if an exemption under state law is clear; nonetheless the opinion may need to assume factual predicates, such as the organizational status of lender, involvement of broker, etc.
 - (c) If there is no statutory exemption, the assurance can present difficult accounting issues, and may require elaborate assumptions and qualifications. See, e.g., TX Real Estate Report.
2. Choice of law.
 - (a) Challenging issues are presented when the real estate collateral is located in one state, and the lender in another.
 - (b) Restatement of Conflicts of Laws § 187 is helpful, if it reflects the law in both jurisdictions.
 - (c) However, existence of trumping or competing state policies (e.g. anti-deficiency legislation, usury laws) is a factual/legal question that may require knowledge of foreign jurisdiction's law.
 - (d) The conventions of the Accord can be helpful.
3. Personal property security interest (UCC) opinions.
 - (a) A general enforceability opinion, by broad consensus, covers only the contractual elements of a security agreement, as opposed to creation, attachment, perfection or priority of a security interest.
 - (b) Security interest opinions are justifiable only if personal property is an important part of the collateral.
 - (c) There are difficulties with substantive opinions; some believe that the assumptions and qualifications are so extensive as to make the opinion a useless, or even a misleading, assurance.
 - (d) It can be argued that transaction costs are better spent on UCC file searches, or for the cost of UCC title insurance.

4. Assignments of rents.
 - (a) The typical provision requires loan default as a condition to collection or other enforcement by the lender; some view an assignment of rents as a hybrid real estate/personal property collateral asset.
 - (b) The normal method of enforcement is the equitable remedy of receivership, which is highly discretionary, and therefore subject to equitable principles exception. In some states (e.g., CA). enforceability opinions are given by referring to a process prescribed by statute.
 - (c) The ability to give the opinion, and qualifications, are a function of local law; the issues include whether state law (or a federal bankruptcy court) adopts a lien theory or title theory of encumbrance, whether the assignment is "absolute" or an assignment for security purposes, etc.
 - (d) Assignments of the right to receive rents owed by the US government raise special issues.
5. Guaranties.
 - (a) Enforceability issues regarding waivers of suretyship defenses are problematic and not adequately covered by the equitable principles exception.
 - (b) "Upstream" and "sidestream" guaranties (e.g., collateral provided by a parent or affiliate entity) present special concerns, which may be covered by the bankruptcy (fraudulent conveyances) exception.
 - (c) The generic exception is not helpful, since potential exoneration defenses may totally nullify the obligations of the guarantor.
 - (d) See the discussion of appropriate qualifications in the Arizona, California, New York and other real estate reports.
6. Environmental indemnities.
 - (a) Issues, not exclusive to real estate, exist regarding enforcement of indemnities in general.
 - (b) When given by a third party, the indemnity is in essence a guaranty, raising the same issues (see discussion above).
 - (c) State anti-deficiency legislation limiting collection of the debt after foreclosure of collateral may affect enforceability. (See CA statute.)

D. Opinions That Generally Ought Not Be Requested or Given.

1. Opinions regarding title to property, the effectiveness of a mortgage lien, exceptions to title, etc. are inappropriate. These issues are covered by title insurance.
2. Land use opinions involve factual and technical issues that are unlike other legal opinions, and are typically addressed by certificates or reports from architects, engineers and public agencies.
3. Environmental opinions are similar to land use opinions and are generally not appropriately requested or given.

E. Typical Entity Opinions with Special Implications for Real Estate Transactions:

1. The opinion that the borrower is qualified to do business locally (and elsewhere).
 - (a) Broad qualification opinions rarely are required for mortgage loan transactions.
 - (b) Where required, such opinions are usually confined to the state where the borrower does business and, if legally required, the location of collateral.
2. Non-contravention opinions; i.e., there are no conflicts with or violations of:
 - (a) Organizational documents (see also, due authorization opinions).
 - (i) Where the borrower is a single purpose, recently formed entity, there is rarely an issue. Where the entity is a multi-purpose operating company, the analysis may be more complex.
 - (ii) A working knowledge of applicable law governing limited liability companies (LLC's), the real estate ownership entity of choice, will be necessary; sometimes partnerships, corporations and other entities as well.
 - (b) Other agreements of borrower.
 - (i) In addition to the usual concerns regarding violations of financial covenants, etc., there are special real estate issues which arise regarding the applicability and enforceability of due on sale or due on encumbrance provisions.
 - (ii) An opinion should avoid application to "performance" of documentary obligations (which might require, for example, consents per various documents affecting the property); i.e., it should be limited to "execution and delivery" of loan documents.
 - (c) Court orders or decrees.

- (i) Do these include administrative land use proceedings, etc.?
 - (ii) Use of client certificates to identify court orders, etc., is comparable to non-real estate practice.
- (d) Laws, regulations, government restrictions.
- (i) Note familiar concerns regarding implied land use opinions.
 - (ii) Opinions should be limited to the execution and delivery of documents, not performance of obligations.
 - (iii) The potentially expansive meaning of the opinion can be dangerous, given the often minimal due diligence undertaken by opining attorneys; a knowledge qualification is an ineffective limitation.
 - (iv) Many lawyers insist on limiting the opinion to specified laws of concern to the lender.
 - (v) Opinions that the client is in compliance with all laws affecting the client, its business or its property are inappropriate.
3. All requisite consents and approvals have been obtained.
- (a) Note the risk of an implied land use opinion (see above).
 - (b) The opinion should be limited to execution and delivery (not "performance") of loan documents.
 - (c) Opinions that the client possesses all licenses, permits, etc. necessary to the conduct of its business or the operation of the client's property are inappropriate.
4. No pending litigation.
- (a) This opinion presents the same due diligence issues as business opinions; i.e., need to define knowledge and scope of investigation.
 - (b) Does litigation include various formal and informal land use proceedings and permit processes?
 - (c) What matters affect the property? Litigation, administrative proceedings and other proceedings that may affect real property collateral do not always name the borrower.
 - (d) Compare audit response letters given to accountants.

F. ABA/ACREL Annotated Opinion Project.

1. What subjects should a nationally sponsored annotated opinion address?
 - (a) General procedural and introductory matters.
 - (i) Documents reviewed, scope of review, due diligence.
 - (ii) Jurisdictional limitations.
 - (iii) Client consent.
 - (iv) Disclosure of financial interests.
 - (v) Reliance on opinions of other counsel.
 - (vi) Local counsel opinions.
 - (vii) Updating of opinions.
 - (b) Appropriate or customary scope of opinion letter requests.
2. What opinions and qualifications should be included and discussed in the Annotated Opinion? (See above).
3. What is the appropriate format for an Annotated Opinion?
 - (a) Alternatives include:
 - (i) A fully articulated model opinion with lengthy footnotes (cf., 1998 New York Mortgage Report; 2008 Pennsylvania Report, etc.).
 - (ii) A discursive commentary regarding the issues, with a standard form opinion as an Appendix (cf., 2004 Arizona Bar Report, 1997 Georgia Real Estate Secured Transactions Report, etc.).
 - (iii) A short form opinion with provisions incorporated by reference (cf., 2007 Maryland Bar Report; ABA Business Law Accord, etc.).
 - (b) The tentative decision of the Steering Committee is to use the ABA/ACREL Inclusive Opinion with extensive footnotes.
4. What is the appropriate process for identifying a national consensus on varying issues, where one exists, and at the same time allowing for variations of approach based on local Customary Practice?
 - (a) Again, the tentative decision of the Steering Committee is to review the most commonly referenced state bar reports as a basis for identifying consensus, while noting examples of contrary local practice in the various reports.

- (b) Should the joint ABA/ACREL Annotated Opinion suggest "best practices" where no clear consensus exists?

G. Resources.

1. ABA/ACREL Real Estate Opinion Letter Guidelines (2003).
2. ABA/ACREL Inclusive Opinion Report (1998).
3. ABA/ACREL Accord Adaptation Report (1993).
4. ABA Business Law Opinion Accord (1991).
5. Various State bar real estate reports.