# In Our Opinion

## The Newsletter of the Legal Opinions Committee

**ABA Business Law Section**

**Volume 17 — Number 2**

**Winter 2017 - 2018**

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**James F. Fotenos and Susan Cooper Philpot, Editors**

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FROM THE CHAIR

I am pleased to share with you the Winter 2017-2018 issue of In Our Opinion. It includes the usual wealth of information about the work of our Committee and other substantive committees in which many of our members participate. And it includes a new segment “Recent Developments on Twitter.” While luddites like me are still looking for a twitter switch on analog devices, others are finding “@ABALegalOpinion” a very useful tool for keeping current on legal opinion developments. I want to thank the Social Media Committee (Rick Frasch, Christina Houston and Anna Mills) for moving this initiative forward.

Let me direct your attention to Jim Fotenos’ article “Rethinking the Validly Issued Opinion on Equity Interests Issued by Alternative Entities.” Jim was co-chair of a working group comprised of representatives of the Partnerships and Limited Liability Companies Committee of the Business Law Section of the State Bar of California that prepared a 2016 report, “Third-Party Closing Opinions: Limited Liability Companies and Partnerships” (posted to our Committee’s Legal Opinion Resource Center). TriBar is also finalizing for publication its report, “Third-Party Closing Opinions: Limited Partnerships.” So this is a busy time for those of us who work on opinions covering limited partnerships and limited liability companies. I expect Jim’s article to be the first in a series. I know that Jim has debated some of his positions with other experts in this area and, as with most of the topics dealt with by our Committee, consensus, let alone unanimity, remains an elusive goal. So I look forward to more content on these topics and hope this Newsletter will become the hub for debate on this important area of opinion practice.

Spring Meeting. If you live in areas where Winter still grips, you must be looking forward to Spring. What better place to celebrate its arrival than in Orlando? So please do not forget to register for the ABA Business Law Section’s Spring Meeting, April 12-14. And while you are thinking of it, please publicize the meeting among your colleagues – we learn from each other and seeing new, younger members in Orlando will further warm everybody’s heart (particularly the Section’s leaders…). You will find on the next page a schedule of the meetings and programs that may be of interest to members of our Committee, as well as a link to the full schedule.

Chair’s Reflections. I find it hard to believe that I am approaching the half-way point of my term as chair. So I am going to take a moment to reflect on what our Committee is doing, hoping to stimulate thoughts as to what else we should be doing. As I tried to organize my thoughts, I recalled an exchange with my partners about the risks law firms face in certain areas of practice. Those who serve as our firm’s gatekeepers on third-party legal opinions deal with the risks implicated by giving them every day and are therefore often thought of as de facto “risk management committees.” While that may not be totally apt, it is true that we are well versed in risk mitigation policies and practices. Opinion practice involves first and foremost the risk of being wrong in reaching legal conclusions under the covered law. While we face that risk in advising our clients, it feels different when we give opinions to non-clients. We spend a lot of time in our Committee dealing with those differences and with the tension created by the fact that our clients pay us to have an adversarial relationship with the same parties to whom they then ask us to give opinions on their behalf. The reasons for this arguably illogical practice are deeply embedded in the U.S., and that practice is not likely to be discontinued any time soon.

Statement on Opinion Practices. So at the core of the work of our Committee is customary practice – both customary diligence that opinion givers ought to exercise and customary usage of terms used in third-party opinions. The ongoing joint project of our Committee and the Working Group on Legal Opinions on the Statement of Opinion Practices (the “Statement”) and the Core Opinion Principles, a concise statement of

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key opinion principles drawn from the Statement that is designed to be attached to or incorporated by reference in opinion letters, is a key effort. The joint committee has been working hard on the Statement to achieve consensus, with the goal of obtaining the broadest possible adoption of the Statement by bar groups across the country. While many (including me) had hoped to see the Statement reach the final approval stage faster than has turned out to be the case, the extra time and effort are well spent if they will result in a better and more broadly supported document.

Survey of Opinion Practice. A third critical piece of our Committee’s work is to document what practicing lawyers actually do and how law firms set and administer policies and procedures on third-party legal opinions. We all hold fast to two key elements of “the creed” for our Committee: do no harm and abide by the golden rule. Having accurate, fresh information on prevailing practice is critical, and we owe a huge thank you to our Committee’s Survey of Opinion Practices Task Force for the work they are doing to get the next survey ready for circulation. This task force will be meeting in Orlando.

Cross-Border Opinion Practice. Equally important is to keep our Committee’s work relevant as practice evolves. Many more U.S. lawyers find themselves dealing with cross-border transactions. The publication in 2015 of our Committee’s report on “Cross-Border Closing Opinions of U.S. Counsel” (71 Bus. Law. 139 (Winter 2015-2016)) provided guidance in this area. Now we are working on “version 2.0” of the cross-border opinions project: seeking convergence among lawyers from different countries so the process of negotiating and giving opinions in cross-border transactions becomes less contentious and costly. The U.S. and England used to be thought of as the only choices for the law governing financing transactions. But that is changing as more jurisdictions have connections to the deals. This introduces a further risk: opinions now travel not only across a table when everybody speaks the same language, both literally and figuratively, but increasingly across tables where variables and pitfalls amplify the challenges for opinion givers. Our Committee’s Cross-Border Opinions Task Force is working to explore customary usage of terms, including widely accepted qualifications, exceptions and assumptions, across jurisdictions to reduce the risk of misunderstanding from differences in law and practice, as well as language barriers. This task force will be meeting in Orlando and there will also be a program in Orlando on Thursday, April 12 (4:00 p.m. – 5:30 p.m.) where a panel of expert practitioners from England, The Netherlands and Canada, as well as the U.S., will explore these topics.

A Proper Balance. Finally, a tenet of opinion practice is that third-party legal opinions not be devices to shift risk from the principals in a business transaction onto the lawyers. The principle that the opinion process should not be approached as a game in which one side wins and the other side loses has become settled, but the temptation is there: if there are legal uncertainties the parties cannot resolve or an area of law that involves poorly understood legal risks, why not ask for language in a closing opinion that bridges the gap? Our Committee works to counter this temptation by developing balanced guidance so there is more consensus and a better understanding of what opinion recipients are entitled to get and opinion givers can reasonably be expected to give. One area where we identified a particular need for such guidance is opinions covering intellectual property issues in capital markets and other financing transactions. Our Committee’s Intellectual Property Opinions Joint Task Force is working on that project and will be meeting in Orlando.

Expanding Our Horizons. The cross-border and IP opinions projects also represent avenues for expanding the horizon of our Committee. U.S. and non-U.S. lawyers who work on cross-border transactions and lawyers who advise IP-rich growth companies will hopefully come to appreciate the contributions our Committee can make and become active in our work. Recent headlines have alerted us to a declining
participation in the ABA generally. While that topic is well above my pay grade, I suspect that adding projects that address real, practical needs within the profession and producing content that is fresh and relevant to new segments of practice is one way to counter this negative trend. It is all of a piece: revisiting old principles of customary practice, gathering new survey data, engaging with lawyers globally and staying relevant to the fastest growing segments of law practice – and then writing about it in articles, reports and on Twitter.

So this is my “mid-term inventory” of projects. As always I welcome all constructive criticism and suggestions for making the work of our Committee – which means the generous efforts of the many among our Committee’s members who volunteer their time and energy – more effective. I hope to see many of you in Orlando.

- Ettore A. Santucci, Chair
  Goodwin Procter LLP
  esantucci@goodwinprocter.com

**Legal Opinions Committee**

**Thursday, April 12, 2018**

4:00 p.m. – 5:30 p.m.

**Friday, April 13, 2018**

Survey of Opinion Practices Task Force:
7:30 a.m. – 9:00 a.m.

Cross-Border Opinions Task Force:
9:00 a.m. – 10:30 a.m.

Committee Meeting:
3:30 p.m. – 5:00 p.m.

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1 The URL is
Legal Opinions Committee (continued)

Friday, April 13, 2018

Reception: 5:00 p.m. – 6:00 p.m.
(Sponsor: Akerman LLP)

Saturday, April 14, 2018

Intellectual Property Opinions Joint Task Force:
11:00 a.m. – 12:00 p.m.

Securities Law Opinions Subcommittee,
Federal Regulation of Securities Committee

Friday, April 13, 2018

Subcommittee Meeting:
2:00 p.m. – 3:00 p.m.

Law and Accounting Committee

Saturday, April 14, 2018

Committee Meeting:
9:00 a.m. – 10:00 a.m.

Audit Responses Committee

Saturday, April 14, 2018

Committee Meeting:
10:00 a.m. – 11:00 a.m.
The Business Law Section held its Fall Meeting in Washington, D.C. on November 17-18, 2017. The Section had a full complement of meetings and programs. The following are reports on meetings held at the Fall Meeting of interest to members of the Committee on Legal Opinions.

**Legal Opinions Committee**

The Legal Opinions Committee met on Friday, November 17, 2017. There follows a summary of the meeting.

**Statement of Opinion Practices.** Stan Keller and Steve Weise led a discussion of the most recent draft, dated November 7, 2017, of the Statement of Opinion Practices (the “Statement”). The November 7 draft, together with a copy marked against the draft dated March 28, 2017 considered at the Committee’s April 7, 2017 meeting, was posted in advance of the meeting on the Committee’s website.

Stan and Steve emphasized that the revisions reflected in the November 7 draft of the Statement are not intended to make substantive changes to the Statement but to clarify it in response to comments received following the April meeting. The Joint Committee is continuing its work with the objective of obtaining a national consensus supporting the Statement when it is finally adopted.

Stan and Steve reviewed with the Committee the key changes made to the Statement since the April meeting, including the following:

- The section on the presumption of regularity in the earlier draft has been deleted because the Joint Committee concluded that it would be best addressed in the existing *Guidelines for the Preparation of Closing Opinions* (§ 3.3 “Presumption of Regularity”), 57 Bus. Law. 875, 878 (2002).

- The definitions of the terms “knows” and “recognizes” in the earlier draft were deleted so as to leave them to be understood in accordance with their customary meanings.

- Discussion is continuing on Section 12 of the Statement (addressing misleading opinions) and in particular the footnote to that section that amplifies the statement in the text. Several approaches to the footnote are being considered.

A question was raised whether the last sentence of Section 5.5 of the Statement on stated assumptions adequately alerted opinion givers that even with disclosure circumstances may arise in which they might decide not to give an opinion. After discussion, the understanding was that the last sentence of Section 5.5 will be considered further by the Joint Committee.

A question was raised by email subsequent to the meeting about whether the sentence in Section 5.6 identifying no litigation confirmations as an exception to the general rule that factual confirmations should not be requested fails to take into account the trend away from giving no litigation confirmations. That sentence also will be considered further by the Joint Committee.

At the conclusion of the discussion of the Statement, the Committee authorized the Chair in his discretion, once the Joint Committee
agrees on a revised exposure draft of the Statement, to approve the circulation of the draft for review and comment by state bar and other opinion groups, with the expectation that the Statement as revised would be submitted for approval by the Committee at its April 2018 Spring Meeting in Orlando.

Survey of Law Firm Opinion Practices. John Power and Arthur Cohen (Haynes and Boone LLP) are co-chairing a subcommittee of the Committee that is preparing a survey of law firm opinion practices to update the 2010 survey conducted by the Committee (and published in 68 Bus. Law. 785 (2013)). The subcommittee met earlier that morning and is making steady progress. The subcommittee is hoping to be in a position to submit a draft of the survey for approval by the Committee at its April 2018 Spring Meeting in Orlando.

Twitter Report. Rick Frasch is now actively tweeting opinion news and developments (@ABALegalOpinion). The source materials referred to in the tweets are accessible from the Committee’s website under “Twitter Materials.” The Chair and Rick encouraged the members to follow Rick’s tweets and to encourage their colleagues to do likewise.

Task Forces and Programs. The Chair encouraged the members of the Committee to attend meetings of the Committee’s two newly-formed task forces, on cross-border opinions and on intellectual property opinions in capital markets transactions (the latter a joint task force with the Intellectual Property Committee). Both task forces are in their organizational stage and were holding meetings the following morning, November 18.

The Committee sponsored a program on “Opinions on Enforceability of Contract Provisions Allocating Risk to Opinion Givers’ Client” the following morning, November 18. The materials for the program are available on the Business Law Section’s website under “Past Section Meetings/Business Law Section Fall Meeting 2017/Program Materials, accessible here. The materials include sample forms of an exception to an enforceability opinion excluding from its coverage risk allocation provisions (at page 12).

Other. The meeting concluded with brief remarks on the summary judgment granted by the United States District Court for the Central District of California to an opinion giver on claims related to its closing opinion (Gemcap Lending, LLC v. Quarles & Brady, LLP), 2017 WL 4081884 (September 13, 2017 (on appeal)), and the recent opinion of the Delaware Chancery Court limiting the use of Section 204 of the Delaware General Corporation Law to correct defective corporate acts (Nguyen v. View, Inc., 2017 WL 2439074 (Del. Ch. June 6, 2017).

Next Meeting. The next meeting of the Committee will be held at the Section’s Spring Meeting in Orlando, Florida on April 12-14, 2018.

- James F. Fotenos
Greene Radovsky Maloney Share & Hennigh LLP
jfotenos@greeneradovsky.com

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4 The URL is https://www.americanbar.org/content/dam/aba/events/business_law/2017/11/fall/materials/enforceability-201711.authcheckdam.pdf.

5 For a review of the Nguyen decision, see Steve Bigler’s and Stephanie Norman’s article in the Summer 2017 (vol. 16, no. 4) issue of the Newsletter at 4-7. Links to both decisions cited in the text are available at the Committee’s website under “Twitter Materials.”
Audit Responses Committee

The Audit Responses Committee met on Friday, November 17, 2017. The principal discussion points are summarized below.

Update on Law and Accounting Committee. Jeffrey Rubin provided an overview of the topics discussed during the Business Law Section’s Law and Accounting Committee meeting, which immediately preceded the Committee’s meeting.

Report on SEC Release 34-81916 (Oct. 23, 2017). Alan Wilson updated the Committee on the Securities and Exchange Commission’s approval of new PCAOB AS (“Auditing Standard”) 3101 (“The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion”). Mr. Wilson focused on statements in the SEC order and remarks by SEC Chairman Jay Clayton regarding the new standard. Mr. Wilson described three areas of concern with the new standard that were addressed in the SEC’s order, namely that the new critical audit matters (“CAMs”) disclosure will (a) devolve into a recitation of unnecessary boilerplate, (b) introduce information into a company’s periodic reports that was not otherwise disclosed by the company, and (c) chill auditor-audit committee communications. Members of the Committee noted that audit committees should engage with their auditors before AS 3101 becomes effective to evaluate the impact of the new CAM disclosure requirements.6 Members of the Committee also commented on the average number of CAMs that are likely to be reported in an audit report and considered whether the new CAM disclosures would affect the audit letter process. In this regard, members noted that PCAOB expects that auditors, in most audits, will determine that at least one matter involves especially challenging, subjective or complex auditor judgment, which could give rise to a CAM. SEC Chairman Jay Clayton has stated that he would be “disappointed” if the new standard resulted in “defensive, lawyer-driven auditor communications,” suggesting that CAM disclosures should be limited to those matters that are truly critical and satisfy the definition of a CAM. In light of these comments, members of the Committee suggested that attorneys should remain vigilant with respect to possible nonconforming requests in audit inquiry letters as the new CAM disclosure regime becomes effective.

Report on Developments in SEC v. RPM International Inc. Stanley Keller reported on developments in the ongoing SEC enforcement action against RPM International Inc. and its general counsel. In that action the SEC alleges that RPM failed to properly accrue for and disclose a loss contingency related to a government investigation prompted by a qui tam complaint alleging that an RPM subsidiary overcharged the government under government contracts. On September 29, 2017, the D.C. District Court issued its opinion denying the defendants’ motions to dismiss the complaint. See SEC v. RPM International Inc., 2017 WL 4358693 (D.D.C. September 9, 2016).

Mr. Keller noted that the case involves two audit response letters – one from RPM’s general counsel and one from RPM’s outside counsel. The SEC focused on the general counsel’s alleged failure to timely inform RPM’s officers, the audit committee and the independent auditors of the results of RPM’s internal inquiry regarding overcharging and of settlement discussions with the Department of Justice (“DOJ”). Members noted the tension that can exist between a general counsel’s role as company legal counsel and as a member of management. Members also noted that, from a corporate governance perspective, a general counsel’s obligation is to advise the board but also to defer on business decisions to other

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6 AS 3101 will become effective, with the exception of the CAM rules, for all audits of fiscal years ending on or after December 15, 2017. The CAM rules will become effective for audits of large accelerated filers for fiscal years ending on or after June 30, 2019, and for all other companies to which the requirements apply for fiscal years ending on or after December 15, 2020.
members of management, including a company’s chief executive officer.

Mr. Keller referred to his 2016 article, “Dealing with Government Investigations in Audit Responses,” which appeared in the Fall 2016 issue of In Our Opinion. Pointing to his article and the D.C. District Court’s opinion, Mr. Keller discussed the difficult judgment calls that were required with respect to events occurring between the filing of the qui tam suit and RPM’s first disclosure of the action. Members of the Committee noted the challenges in drafting audit response letters when counsel has been provided with a copy of a qui tam complaint but when the government’s investigation remains ongoing and no suit has been filed. The D.C. District Court concluded, based on the facts stated in the pleadings and viewed in the light most favorable to the SEC, that by September 2012, when RPM was aware of the qui tam complaint and had informed the DOJ of an overcharge of at least $11 million, the company’s liability was probable and that a minimum amount of liability was clear. Members of the Committee tended to agree that prior to September 2012, no disclosure likely was required because RPM was unaware whether a claim was being asserted or whether it was probable that one would be asserted. Members noted that most qui tam complaints do not result in a litigated or settled dispute because the government concludes after investigation not to bring an action.

The Committee also addressed the significance of settlement offers when evaluating contingent liabilities under ASC 450-20. While a company is not required to disclose the making of a settlement offer, members of the Committee observed that the existence of a settlement offer creates a presumption that sufficient probability exists to require an accrual or disclosure with respect to the matter. As noted in the D.C. District Court’s opinion, there is a “plausible inference” that it is probable a loss will occur where a company is aware of a qui tam complaint, calculates an amount of liability in excess of $10 million, and begins discussing settlement options with the DOJ.

Report on Recent PCAOB Investor Advisory Group Presentation. Thomas White reported on a discussion held October 24, 2017 at the meeting of the PCAOB Investor Advisory Group (“IAG”) regarding auditors’ consideration of a client’s noncompliance with laws and regulations. An IAG working group has recommended strengthening auditing standards regarding an auditor’s duty to identify and report suspected and/or confirmed illegal acts. The discussion topic was prompted, in part, by the question of “where were the auditors” that commonly arises in the aftermath of financial crises. Mr. White noted that this topic first appeared on the PCAOB’s research agenda in 2016 and remains on its agenda. Mr. White also noted that international standard setters have amended their standards to increase auditor responsibility in this regard. In discussing U.S. standards, Mr. White referred to PCAOB AS 2405 (“Illegal Acts by Clients”), which sets forth the nature and scope of the considerations auditors should give to the possibility of illegal acts by a client. Mr. White noted that the IAG working group took particular issue with many of the requirements under AS 2405 that use a “should” versus a “must” standard. Members of the Committee observed that Section 10A of the Securities Exchange Act of 1934 requires, among other things, that audits include “procedures designed to provide reasonable assurance of detecting illegal acts that would have a direct and material effect on the determination of financial statement amounts.” As the IAG working group noted, however, auditors do not have an affirmative obligation under U.S. standards to ask clients or their attorneys to confirm whether the client has committed any illegal acts.

Some Committee members suggested that the IAG working group may not have fully considered the impact of its position on the protections afforded by the attorney-client privilege. Noël Para commented that some auditors include requests for the lawyer to disclose illegal acts committed by the client. He advised that lawyers should not respond to such nonconforming requests, as doing so would go beyond the scope of the ABA Statement of

Future Committee Discussion Topics/Projects. The Committee briefly discussed ideas for future Committee discussion topics, which could also serve as the basis for future Committee statements. A list of possible topics was circulated at the meeting with the meeting agenda.

Listserve Activity. A summary of recent activity on the Committee’s listserve is included with this issue of the Newsletter.

Next Meeting. The Committee’s next meeting is scheduled for the Business Law Section’s Spring Meeting in Orlando, Florida, April 12-14, 2018.

- Noël J. Para, Chair7
  Alston & Bird LLP
  noel.para@alston.com

SUMMARY OF RECENT LISTSERVE ACTIVITY
MARCH 2017 – NOVEMBER 2017
(AUDIT RESPONSES COMMITTEE)

[Editors’ Note: This summary of listserve activity during the period of March 2017 - November 2017 among members of the Audit Responses Committee does not necessarily represent the views of the Committee or authoritative pronouncements regarding audit response practice, but rather reflects views of individual members of the Committee on current practice topics. The comments referred to below may be viewed by clicking on the “listserve” item on the Audit Responses Committee’s web page.]

Attorney-Client Privilege and ASC 450-20. A Committee member noted that Accounting Standards Codification 450-20 lists “opinions or views of legal counsel . . . .” among the factors management should consider in assessing the probability of the incurrence of a loss. Committee members were asked to share their experiences as to whether they have been successful in avoiding discussions of litigation assessments and limiting their discussions with auditors to factual matters, either (a) stating that these are management determinations under ASC 450-20 (and not something that lawyers are equipped to do), or (b) stating that they have provided their views regarding the lawsuit to the client and that the company’s reserve amount and disclosures are not inconsistent with counsel’s advice.

Responders suggested that attorneys typically limit their discussions with auditors to the scope of the ABA Statement of Policy Regarding Lawyers’ Responses to Auditors’ Requests for Information, 31 BUS. LAW. 1709 (1976) (the “Statement of Policy”), reprinted in ABA BLS Audit Responses Committee, Auditor’s Letter Handbook (2d ed. 2013). Responders also noted case law is conflicting on whether the attorney-client privilege and work product protection cover audit response letters and that attorneys typically take a conservative approach, in line with the many courts that have held that the attorney-client privilege typically is waived with the respect to matters disclosed in an audit response. Reference was made to the Statement of Policy, which states, in relevant part, that “[i]n view of the inherent uncertainties, the lawyer should normally refrain from expressing judgments as to outcome except in

7 Alan J. Wilson, Esq., of Wilmer Cutler Pickering Hale and Dorr LLP, Content Director of the Committee, served as secretary of the meeting and prepared these minutes.

8 The URL is http://apps.americanbar.org/dch/committee.cfm?com=CL965000.
those relatively few clear cases where it appears
to the lawyer that an unfavorable outcome is
either ‘probable’ or ‘remote.’’ Responders also
suggested that information provided orally to the
auditor is likely to be documented in the
auditor’s work papers, which may be subject to
discovery. It was recommended that if an
attorney contemplates going beyond the scope of
the Statement of Policy in his or her response,
the attorney should explain the risk to the client
and do so only with the client’s express consent.
While one responder noted that some clients
have asked attorneys to expand their audit
responses, such cases tend to be the exception.

**Supplemental Audit Letters.** A Committee
member described comments received from an
accounting firm on the final paragraph of an
audit response letter that the member’s law firm
had used in supplemental letters to auditors,
such as in connection with Form 10-Qs:

**Initial Paragraph:** We have been
requested by [name], [title], to update
our response to you dated [early 2017]
initially issued in connection with your
audit of the financial statements of
Company at December 31, 2016.

... 

**Final Paragraph:** This letter is solely
for your information in connection with
your audit of the financial condition of
the Company at December 31, 2016,
and is not to be quoted in whole or in
part or otherwise referred to in any
financial statement of the Company or
related document, nor is it to be filed
with any governmental agency or other
person, without the prior written
consent of this firm.

The accounting firm advised that the last
paragraph must read: “in connection with your
review of the Company’s interim financial
statements at September 30, 2017.” The
accounting firm made the point that the letter is
being provided in connection with a “review,”
not an audit.

Some members advised that it would be
appropriate to tailor the response letter to fit the
particular circumstances. For example, the
update might be provided in connection with
filing a registration statement. This would be
the case whether the update is done as a short-
form or long-form response. Other members
noted the difficulty of providing such
supplemental letters, largely due to the benefits
of strictly adhering to the Statement of Policy
(and their firms’ own internal processes/policies
for responses). Such members noted that their
firms generally either decline or respond with a
statement such as, “Nothing has come to our
attention that would render our [recent audit
response] materially incorrect.” It was noted
that the ABA BLS Audit Responses Committee,
Statement on Updates to Audit Response Letters,
70 Bus. Law. 289 (Spring 2015) (the “Statement
on Updates”), suggests a different form of
response than this type of negative assurance.
The Statement on Updates advises that such a
response should be prepared in accordance with
the Statement of Policy and the Statement on
Updates.

- Alan J. Wilson, Content Director
Audit Responses Committee
Wilmer Cutler Pickering Hale and Dorr LLP
alan.wilson@wilmerhale.com

**COMMENTARY**

**Rethinking the Validly Issued
Opinion on Equity Interests
Issued by Alternative Entities**

A typical closing opinion addressing the
issuance of capital stock reads as follows:

“The Shares [of capital stock] have
been duly authorized and validly issued
and are fully paid and nonassessable.”
TriBar explains the elements of the “duly authorized” component of this opinion as follows:

“The opinion [duly authorized opinion] means that, under the corporation law of the state in which the Company was organized and the Company’s charter, the shares to which the opinion relates (the “Shares”) were (or will be) immediately prior to their issuance included within the shares that the Company had the power to issue. The opinion covers such matters as whether (i) the applicable state corporation law permits shares having the characteristics of the Shares, (ii) the provisions of the Company’s charter relating to the Shares comply with that law and (iii) sufficient authorized shares of the class of which the Shares are a part were available when the Shares were issued.”

TriBar Opinions Report § 6.2.1, 53 Bus. Law. at 648 (emphasis added) (footnote omitted).9

TriBar first addressed this opinion in the context of alternative entities in its Supplemental TriBar LLC Opinion Report: Opinions on LLC Membership Interests (“TriBar LLC Interests Report”), 66 Bus. Law. 1065 (2011). A typical “validly issued” opinion for an LLC reads as follows:

“The [LLC] [Membership] Interests issued by the Company [the LLC] to the purchasers thereof have been validly issued.”

The “duly authorized” component of the typical capital stock opinion is not included in this opinion for alternative entities because LLC statutes, unlike corporation statutes, do not provide for authorized capital or specify the requirements for creating it, and, unlike corporate charters, LLC operating agreements typically do not create a pool of “authorized” LLC interests. TriBar LLC Interests Report, 66 Bus. Law at 1068. Moreover, because an opinion that corporate shares have been “validly issued” could not be rendered if the shares were not “duly authorized,” TriBar Opinions Report, 53 Bus. Law. at 649, including a duly authorized opinion in an issuance opinion on alternative entity equity interests “would only cover matters already covered by the validly issued opinion and thus ordinarily would add nothing of value.” TriBar LLC Interests Report, 66 Bus. Law. at 1068.

On December 9, 2016, the Executive Committee of the Business Law Section of the State Bar of California approved the report entitled “Third-Party Closing Opinions: Limited Liability Companies and Partnerships” (the “CA Entities Opinions Report” or “CA Report”).10 The CA Report was prepared by a working group (the “CA Working Group”) comprised of representatives of the Partnerships and Limited Liability Companies Committee (the “Partnerships & LLCs Committee”) and the Opinions Committee of the Business Law Section, and is an update and restatement of the Partnerships & LLCs Committee’s 1998 and 2000 reports on legal opinions concerning

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9 A state’s corporation law, for purposes of the duly authorized opinion, includes the state constitution where it contains provisions relevant to the opinion. TriBar Opinions Report § 6.2.1 n. 126, 53 Bus. Law. at 648.

10 Effective January 1, 2018, the sections of the State Bar of California split off and became part of the California Lawyers Association (“CLA”), a voluntary bar association. 2017 Stats. ch. 422 (SB 36). See calawyers.org.
California partnerships and LLCs.\textsuperscript{11} In the course of preparing the CA Report, the CA Working Group struggled with the scope of the validly issued opinion for LLC and limited partnership equity interests. In this article, the author, a co-chair of the CA Working Group and a past (2015-2017) co-chair of the California Opinions Committee, identifies these issues and how they are dealt with in the CA Report.\textsuperscript{12}

\textbf{The Scope of the Validly Issued Opinion for Alternative Entities}

There is no controversy about three of the elements of the validly issued opinion on LLC or LP equity interests:

- It confirms that the creation and issuance of the LLC/LP interests satisfy the requirements of the applicable LLC/LP statute and the entity’s articles of organization (in Delaware, the certificate of formation) and operating/limited partnership agreement;
- It confirms that the issuance of the LLC/LP interests complied with any conditions on issuance in the resolution or other action, if any, adopted under the operating/limited partnership agreement approving the issuance; and
- It confirms receipt of the required kind and amount of consideration for the issuance of the LLC/LP interests.

\textit{See TriBar LLC Interests Report, 66 Bus. Law. at 1066-1067; TriBar LP Opinions Report § 4.0.}

What caused the CA Working Group concern is the next element of the validly issued opinion, which the CA Working Group refers to as the “substantive element.” As stated in the TriBar LLC Interests Report:

“As in the corporate context, this opinion [the validly issued opinion] requires that the LLC have the power under the applicable LLC statute, its certificate of formation, and its operating agreement to create interests in the LLC having the terms of the LLC Interests covered by the opinion. Thus, the opinion also confirms that the terms of the LLC Interests do not violate the applicable LLC statute, the LLC’s certificate of formation, or the operating agreement.”

66 Bus. Law. at 1067 (emphasis added).\textsuperscript{13}

TriBar does not further define what “terms” of the LLC interests it refers to which should be examined against the applicable LLC statute, certificate of formation, and the LLC’s operating agreement. At the beginning of its LLC Report, TriBar defines “LLC Interests” by reference to Section 18-101(8) of Delaware’s LLC Act to mean a member’s share of profits and losses and the member’s right to receive distributions of the

\textsuperscript{11} An exposure draft of the Alternative Entities Opinions Report was posted in April 2016 in the Legal Opinion Resource Center of the Legal Opinions Committee of the Business Law Section of the American Bar Association under “Meetings and Other Materials.” The comment period on the exposure draft ran to September 30, 2016. The Report has now been published by the Business Law Section of the California Lawyers Association and is available, both in hard copy and as an e-book, through this link: \url{http://www.cla.legal/sections/business-law/publications/opinion-resources}.

\textsuperscript{12} The views expressed in this article are those of the author and, otherwise than as stated, do not necessarily represent the views of the CA Working Group or the California Opinions Committee.

\textsuperscript{13} In the more recent TriBar LP Opinions Report, TriBar’s emphasis is on “rights” rather than on “terms.” TriBar LP Opinions Report § 4.0.
LLC’s assets. 66 Bus. Law. at 1066 n. 3. TriBar acknowledges that some states, such as New York, use the term “membership interest” in lieu of the term “limited liability company interest,” and that the term “membership interest” includes a member’s rights, if any, to vote and to participate in the management of the LLC. It notes that an “opinion on an LLC formed in a particular state normally uses the same terminology as is used in that state’s LLC statute.” Id. Accordingly, if an opinion giver addresses the valid issuance of “membership interests,” then the opinion giver should look to the governing statute of the covered law state for the elements or “terms” of those membership interests.14


History of the Substantive Element of the Validly Issued Opinion

An opinion that corporate stock has been validly issued cannot be given if issuance of the stock has not been “duly authorized.” The three elements of the duly authorized opinion on corporate stock are listed in the introduction to this article. See TriBar Opinions Report § 6.2.1, 53 Bus. Law. 591, 648.

Items (i) and (ii) of these elements are stated in terms of whether state corporation law permits shares having the characteristics of the shares addressed by the opinion, and whether the provisions of the company’s charter relating to the shares comply with that law. Thus, for example, a duly authorized opinion on preferred stock carrying special voting rights under Delaware law would address whether the DGCL permits preferred shares having such special voting rights and whether the company’s certificate of incorporation creates those special voting rights for the preferred shares in compliance with the DGCL.

The fullest treatment of the substantive element of the duly authorized/validly issued opinion is found in TriBar’s Preferred Stock Opinions Report. The focus of that report is on the duly authorized opinion, not the validly issued opinion, although, as noted above, the validly issued opinion cannot be given if the shares addressed by the opinion have not been duly authorized. Moreover, the elements of the duly authorized opinion have been engrafted onto the validly issued opinion in the TriBar LLC Interests Report because, as noted by TriBar, in the context of the issuance of LLC interests, the duly authorized opinion ordinarily adds nothing of value to the validly issued opinion. TriBar LLC Interests Report § 1.0, 66 Bus. Law. at 1068.

As one of the elements of the duly authorized opinion on preferred stock, TriBar repeats, very closely, the substantive element of the duly authorized opinion from the TriBar Opinions Report:

“...the Company has the power under the applicable state corporation statute and its charter to create stock having the rights, powers and preferences of the stock in question.”

TriBar Preferred Stock Opinions Report, 63 Bus. Law. at 923.

In interpreting this element of the duly authorized opinion, TriBar, in its Preferred Stock Opinions Report, casts the inquiry in negative terms: because most corporation statutes contain broad statutory authority to create and issue stock with whatever economic

14 Similarly, in its report addressing the substantive element of the valid issuance opinion for LP interests, TriBar acknowledges that limited partnerships formed in states other than Delaware may not have the broad discretion Delaware limited partnerships have to determine the rights of holders of their LP interests, and that, in those states, state bar association reports may provide guidance on which of those rights are covered by a validly issued opinion. TriBar LP Opinions Report § 4.0.
and other terms a corporation chooses, “an opinion preparer’s inquiry regarding this element often will be limited to whether any of the specified rights, powers or preferences of the preferred stock violate provisions of the corporation statute or the company’s charter.” 63 Bus. Law. at 923-924 (emphasis added).

TriBar provides examples of what such a violation might be:

- The preferred stock purports to deny holders voting rights when the charter prohibits non-voting stock; or

- The preferred stock is granted priority in liquidation over an existing class or series whose terms prohibit creation of stock with a higher priority.

63 Bus. Law. at 924.

TriBar concludes its Preferred Stock Opinions Report with additional examples that might cause opinion preparers to qualify their duly authorized opinion on preferred stock:

- The charter establishes a procedure for declaring dividends that contravenes the corporation statute;

- The charter eliminates statutory appraisal rights either by expressly denying those rights or by requiring all holders to vote in favor of a matter if a majority of a class or series so votes (“drag-along rights”) when under the applicable state corporation statute such a requirement constitutes an impermissible advance waiver of appraisal rights;

- The charter provides for a lower percentage vote for approval of certain matters than the vote required by the statute;

- The charter gives holders of a class of stock the right to designate a member of a committee of the board when the statute authorizes only the directors to appoint members of committees of the board; or

- The board pursuant to blank check authority creates a class of stock that is non-voting when a provision in the charter only permits the creation of voting stock.

63 Bus. Law. at 926.

Reading TriBar’s statements together, TriBar describes the substantive element of a duly authorized opinion on preferred stock as whether the company “has the power” under the applicable state corporation statute and its charter to create stock having the rights, powers and preferences of the stock in question, and then indicates that the opinion preparers’ inquiry regarding this element often will be limited to whether any of the specified rights, powers or preferences of the preferred stock violate...
provisions of the corporation statute or the company’s charter.\footnote{16}

TriBar, for understandable reasons, does not use the phrase “rights, powers and preferences” from its Preferred Stock Report in its LLC Interests Report. Instead, it uses the phrase “terms,” without definition or explanation. The Delaware LLC Act does not use this word in describing the interests of members of a Delaware LLC, although it does use the phrase “rights, powers or duties” in describing the powers of a Delaware LLC to create classes or series of members and managers. Del. LLC Act, Del. Code, tit. 6, §§ 18-215, 18-302. Certainly a not unreasonable interpretation of “terms” is that it refers to all of the rights, powers, and duties associated with LLC interests.\footnote{17}

The Delaware LP Act similarly does not use the phrase “terms” when discussing LP interests but, like the Delaware LLC Act, refers to “rights, powers and duties” in describing the powers of a Delaware LP to create classes or groups of limited partners. Del. LP Act, Del. Code, tit. 6, § 17302(a). In its recent report on LP opinions, TriBar focuses on “rights” as the focus of the validly issued opinion rather than on “terms.” See note 5.

TriBar cites, in support of its application of the substantive element of the validly issued opinion to LLC interests, the Preferred Stock Opinions Report.\footnote{18} It is also not unreasonable for opinion preparers to conclude that the “terms” referred to in the TriBar LLC Interest Report include the type of “terms” of preferred stock given as examples in the Preferred Stock Opinions Report as illustrative of the substantive element of the duly authorized opinion, cited in the bullet point paragraphs above. Such “terms” would include the voting rights granted to the members of the LLC, the economic terms of the LLC interests, the priorities or preferences granted to separate classes or series of interests, the dissenters’ rights, if any, granted to the holders of the LLC interests, and the governance provisions (e.g., the procedures to be followed for declaring distributions, the votes or consents for actions required to be approved by the members, and any rights given to a class of members to designate the manager(s) of the LLC) established by the LLC’s operating agreement affecting the membership interests.

The use of the word “terms” to describe LLC interests in the TriBar LLC Interests Report might be cabined by reference to the statutory definition of “LLC interests,” which are defined in that Report by reference to the Delaware LLC Act’s definition of “limited liability company interest”: a member’s share of profits and losses and right to receive distributions of assets. DE LLC Act § 18-101(8) Under this reading, the only “terms” of LLC interests that opinion preparers would need to confirm do not violate

\footnote{18} TriBar also refers to the Preferred Stock Opinions Report at the beginning of its discussion of the validly issued opinion on LP interests in the TriBar LP Opinions Report § 4.0.
the Delaware LLC Act, the LLC’s certificate of formation, or its operating agreement would be the rights to distributions and profits and losses associated with the LLC interests, what are referred to under California’s LLC Act as “transferable interests.” (See note 19 below.) However, this narrow usage of LLC interests is not repeated or highlighted in TriBar’s discussion of the validly issued opinion on LLC interests in the TriBar LLC Interests Report or in its recent TriBar LP Opinions Report and, were this the scope of the substantive element of the validly issued opinion, then the citation to the Preferred Stock Opinions Report would not be necessary. Moreover, were this the appropriate reading of TriBar’s reference to “terms” in its LLC Membership Interests Report, then it would be reasonable to expect this interpretation of terms to be stated explicitly in the Report.

What “Terms” and “Rights” are Addressed by the Substantive Element of the Validly Issued Opinion?

As part of its CA Alternative Entities Opinions Report, the CA Working Group prepared a sample closing opinion illustrating the opinions addressed by the CA Report. The form of the CA Working Group’s sample opinion on the validly issued opinion reads as follows:

“The Membership Interests issued by the Company to the purchasers thereof have been validly issued.”

California’s LLC Act defines “membership interest” to mean “a member’s rights in the limited liability company, including the member’s transferable interest, any right to vote or participate in management, and any right to information concerning the business and affairs of the limited liability company provided by this title.” California Revised Uniform Limited Liability Company Act (“CRULLCA”), Cal. Corp. Code § 17701.02(r).19

The issue that the CA Working Group grappled with is what “terms” of LLC “membership interests” (or, for limited partnerships, its LP interests) are properly understood to be addressed by the validly issued opinion? Do the terms addressed by the validly issued opinion include all of the “rights” granted to the members (or limited partners) by the operating or partnership agreement? Does it include all “duties” imposed upon the members or limited partners by the membership or partnership agreement (e.g., the obligation to respond to capital calls)? Does the opinion subsume whether any of those “terms,” as defined, violate the applicable provisions of the governing statute, for California LLCs, the CRULLCA or, for limited partnerships, the California LP Act (the Uniform Limited Partnership Act of 2008, Cal. Corp. Code § 5900 et seq.)?

TriBar uses the broadly enabling Delaware statutes as its model in describing the substantive element of the validly issued opinion to be whether the terms of the interests violate the relevant provisions of the statute or the company’s governing documents. But what if the enabling statute is not broadly “enabling,” but contains numerous prohibitions on the permissible “terms” that the members or partners of an LLC or LP may adopt? California provides an example of this category of statutes.

1. California’s Alternative Entity Statutes.

While California’s LLC statute professes fealty to the principle of freedom of contract and to the enforceability of operating agreements, e.g., CRULLCA, Cal. Corp. Code § 17701.07(a), CRULLCA contains extensive restrictions on the freedom of members to craft operating agreement terms of their choosing.

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19 “Transferable interest” is, in turn, defined as the right to receive distributions from an LLC in accordance with the operating agreement. Cal. Corp. Code § 17701.02(aa).
Thus, Cal. Corp. Code § 17701.10, contains at least 19 restrictions on the freedom of members to modify the default provisions of CRULLCA, many with subparts and most with extensive cross references to the operative provisions of CRULLCA, many of which are themselves complex. Many of the restrictive provisions require judgments to be made as to what is “unreasonable” or what constitutes “informed consent.”

For example, the operating agreement of a California LLC may not:

- Eliminate the duty of loyalty, the duty of care, or any other fiduciary duty, but the operating agreement may narrow fiduciary duties in specified ways, Cal. Corp. Code §§17701.10(c)(4), 17701.10(c)(14),(15), 17701.10(d), 17701.10(g);
- Eliminate the obligation of good faith and fair dealing between a member or manager and the members, but the operating agreement “may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable …” (Cal. Corp. Code §17701.10(c)(5));
- Vary the duties of an LLC to maintain and provide copies of the information, returns, and reports required by CRULLCA, Cal. Corp. Code §§17701.10(d)(2), 17704.10(h);
- Except as permitted by CRULLCA, vary the rules on winding up and dissolution of an LLC stated in Cal. Corp. Code §17707.01 – 17707.09 (Cal. Corp. Code §17701.10(c)(8));
- Unreasonably restrict the right of a member to maintain a class action or derivative action against the LLC, Cal. Corp. Code §17701.10(c)(9);
- Vary any of the merger or conversion rules of Article 10 of CRULLCA (§17710.01 – 17710.18), Cal. Corp. Code §17701.10(c)(10), (12);
- Unreasonably reduce the duty of care of a member or manager to the members, Cal. Corp. Code §17701.10(c)(15);
- Vary the agency rules applicable to members and managers, Cal. Corp. Code §17701.10(d); and
- Eliminate or limit a member’s or manager’s liability to an LLC for money damages, except in one of five specified ways set out in Cal. Corp. Code § 17701.10(g).

In addition, CRULLCA requires that any modification of the fiduciary duties of the manager to an LLC and its members must be with the “informed consent” of the members of the LLC, Cal. Corp. Code § 17701.10(e).


While California’s list of restrictions on the freedom of members to craft an operating agreement of their choice is extensive, it is not unique. Section 110 of the Revised Uniform Limited Liability Company Act (2006) prepared by the National Conference of Commissioners on Uniform State Laws (derived from Section 103 of the 1996 version of the Uniform LLC Act) contains eleven separate prohibitions on what may be included in an operating agreement (§ 110(c)), five separate categories of provisions that may be included in an operating agreement if “not manifestly unreasonable” (§ 110(d)), and additional restrictions on the power of members to select operating agreement provisions of their choice (§ 110(e)-(g)). Versions of NCCUSL’s model act had been enacted in 15 states and are pending in four more.

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3. Delaware’s LLC Act.

California’s and the Uniform Act’s approach should be contrasted with Delaware’s, whose LLC Act contains no such provisions. Section 18-1101 of Delaware’s LLC Act articulates Delaware’s policy “to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements” and permits drafters of Delaware LLC operating agreements wide latitude in the provisions they may include in a Delaware LLC agreement, including provisions that restrict or eliminate fiduciary duties. The only restriction in Section 18-1101 is that a Delaware operating agreement “may not eliminate the implied contractual covenant of good faith and fair dealing.” Del. Code, tit. 6, § 18-1101(c), (e).

While the freedom granted by Delaware’s LLC Act to the drafters of Delaware LLC operating agreements is wide, it is not unbounded, as illustrated by Vice Chancellor Laster’s opinion in In re Carlisle Etcetera LLC, 114 A.3d 592 (2015). In this decision on a motion to dismiss, the Vice Chancellor ruled that, notwithstanding that the petitioner assignee of a two-member Delaware LLC had no contractual right under the LLC’s operating agreement to seek dissolution of the LLC under Section 18-802 of Delaware’s LLC Act (because the assignee had not been admitted as a member), the petitioner had standing to seek dissolution by invoking the equity jurisdiction of the Chancery Court. Harkening back to commentaries on equity by Story and Pomeroy, the Vice Chancellor concluded that the petitioner could seek dissolution of an LLC in equity notwithstanding any provision of the LLC agreement to the contrary or petitioner’s lack of standing to invoke the statutory dissolution provisions of the Delaware LLC Act. 114 A.3d at 601-607.

Assume a Delaware LLC operating agreement contains an express waiver of the members’ rights to seek dissolution and the appointment of a receiver under the applicable provisions of the Delaware LLC Act per R & R Capital. Should an opinion giver, in delivering a validly issued opinion on membership interests issued by such an LLC, take a qualification in view of Vice Chancellor Laster’s opinion in Carlisle? Can the opinion giver conclude that the “terms” of the membership interests for purposes of the validly issued opinion do not extend to waivers of the right to seek dissolution of the LLC?

Similar freedom, with the same limitation, is granted to the partners of a Delaware limited partnership. See Del. Code, tit. 6, § 17-1101(c), (d).

21 In so concluding, the Vice Chancellor distinguished Chancellor Chandler’s unpublished decision in R & R Capital, LLC v. Buck & Doe Run Valley Farms, LLC, 2008 WL 3846318 (Del. Ch. 2008), in which the Chancellor squarely held that members of a Delaware LLC could waive their rights to seek dissolution and the appointment of a receiver under the Delaware LLC Act.

22 Based upon the listing of preferred stock “rights, powers and preferences” that might cause opinion preparers to qualify their duly authorized opinion on preferred stock, an opinion giver probably could not reach this conclusion. See, e.g., the example from the TriBar Preferred Stock Opinions Report of a charter provision eliminating statutory appraisal rights when under the applicable state corporation statute such a provision would constitute an impermissible advance waiver of appraisal rights. TriBar Preferred Stock Opinions Report, 63 Bus. Law. at 923.

Assume a Delaware LLC operating agreement contains an express waiver of the members’ rights to seek dissolution and the appointment of a receiver under the applicable provisions of the Delaware LLC Act per R & R Capital. Should an opinion giver, in delivering a validly issued opinion on membership interests issued by such an LLC, take a qualification in view of Vice Chancellor Laster’s opinion in Carlisle? Can the opinion giver conclude that the “terms” of the membership interests for purposes of the validly issued opinion do not extend to waivers of the right to seek dissolution of the LLC?

23 If a provision would in all circumstances be held unlawful, the equitable principles limitation would not apply. The equitable principles limitation is contextual, and includes those principles that courts apply when, in light of the particular facts occurring after the effectiveness of an agreement, the courts decline in the interest of equity to give effect to a particular provision of the agreement. See TriBar Opinions Report § 3.3.4, 53 Bus. Law. at 625.

24 Similar freedom, with the same limitation, is granted to the partners of a Delaware limited partnership. See Del. Code, tit. 6, § 17-1101(c), (d).
confront in addressing the substantive element of the validly issued opinion for alternative entities, even in a jurisdiction as accommodating to the drafters’ choices as Delaware.


The variation in states’ alternative entity statutes is crucial to a determination of the usage and diligence associated with the validly issued opinion on equity interests of alternative entities. As TriBar acknowledges, the elements (or “terms”) of the “interests” of an LLC or LP addressed by the validly issued opinion is a function of the covered state’s (i.e., the state whose law is covered by the opinion letter, which usually would be the state of organization) alternative entity statute. Whether those elements or terms, as articulated in the LLC’s or LP’s governing documents, violate the governing statute is heavily dependent upon whether and how that statute restricts the freedom of the members and partners of the LLC or LP to craft terms of their choosing. The more restrictions on that freedom imposed by the governing statute, the more complex the opinion preparers’ task is in addressing the substantive element of the validly issued opinion. Because of this variation, and in the absence of definitive guidance, there can be no national common understanding of the scope of the substantive element of the validly issued opinion or the diligence required to render the opinion — this usage and these tasks are to be determined state-by-state.

Addressing the Ambiguity in the Scope of the Substantive Element of the Validly Issued Opinion in the Context of LLCs and LPs

One obvious solution to the challenges posed by the validly issued opinion on LLC and LP interests is to include an explicit limitation to the scope of the opinion. The limitation would define those “terms” or “rights” of the interests being addressed by the opinion. For example, the opinion giver may expressly define the terms being addressed by the opinion as only those terms governing the members’ (or limited partners’) rights to distributions and rights to vote, two clearly core “terms” or “rights” of equity interests in LLCs and LPs. By such a limitation the opinion giver would make clear that it is addressing whether the distribution and voting rights provisions of the operating or limited partnership agreement violate the applicable governing statute or certificate of formation of the entity, but is not addressing in a similar fashion any other rights or duties of the members or limited partners set out in the membership or partnership agreement. The scope of the opinion would be determined by the opinion giver, based upon the context in which the opinion is to be delivered and the expectations of the opinion recipient (and might include, for example, in addition to the rights to distributions and voting rights, information rights).

In its treatment of the validly issued opinion on LLC and LP interests, the California Alternative Entities Opinions Report recommends that opinion preparers consider two alternative forms of an express limitation to the opinion. The first follows the alternative mentioned in the previous paragraph, and limits the substantive element of the opinion to whether the members’ (or limited partners’)

Any limitation on the validly issued opinion would likely not be accepted in an Exhibit 5 opinion required in connection with the issuance of LLC or LP interests in an SEC-registered offering of the same. See Securities and Exchange Commission, Legality and Tax Opinions in Registered Offerings (Staff Legal Bulletin No. 19) (October 14, 2011), 2011 WL 4957889 at **2, 11. Historically alternative entities that have registered their offerings of equity interests have been Delaware alternative entities. As noted above, satisfying the substantive element of the validly issued opinion for Delaware alternative entities does not pose the challenges confronted under California’s and other states’ alternative entity statutes following the uniform act model. Moreover, given the amounts inevitably involved in an SEC-registered offering, the necessary diligence required to give an Exhibit 5 opinion for a registered offering may very well be cost-justified even if the relevant “terms” to be addressed by the opinion are given the broadest interpretation under the Delaware alternative entity statutes.
rights to distributions and rights to vote violate the applicable statute or the governing documents of the entity:

“Our opinion in paragraph ___ above [the valid issuance opinion] confirms that the issuance of the Membership [LP] Interests satisfies the requirements of RULLCA [the LP Act] and the Company’s Articles of Organization [Certificate of Limited Partnership] and Operating [Limited Partnership] Agreement, including any necessary approvals by the manager[s] and members [general partner[s] and limited partners] of the Company and the receipt of the amount and kind of consideration, if any, required thereunder. The opinion also confirms that the provisions of the Company’s Operating [Limited Partnership] Agreement governing distributions do not violate RULLCA [the LP Act] or the Company’s Articles of Organization [Certificate of Limited Partnership], and that the Company’s Operating [Limited Partnership] Agreement does not purport to deny the manager[s] and members [general partner[s] and limited partners] of the Company any of those non-waivable voting [approval] rights mandated by RULLCA [the LP Act]. The opinion does not otherwise address, and we express no opinion on, whether any of the other provisions of the Operating [Limited Partnership] Agreement violate RULLCA [the LP Act] or the Articles of Organization [Certificate of Limited Partnership].”


In crafting this limitation, the CA Working Group sought to balance the interests of opinion givers for a sensible limitation on the scope of the substantive element of the validly issued opinion and the interests of opinion recipients in receiving, at a minimum, assurance that the validly issued opinion on LLC or LP interests addresses whether the governing documents’ treatment of distributions and voting rights violate the statute governing the entity or its charter.

Furthermore, expressly limiting the scope of the substantive element of the validly issued opinion on alternative entity equity interests also responds to the belief of several members of the CA Working Group that the substantive element of the validly issued opinion should only focus on those terms which, if found violative of the governing statute, would permit the purchasers of the equity interests to rescind their purchases. Conversely, terms of the interests that would not permit purchasers to rescind their purchases should not be addressed by the substantive element of the validly issued opinion. The law of rescission supports this bifurcation. See, e.g., CA Civil Code § 689(b)(4) (permitting rescission of a contract if, inter alia, the consideration for the obligation of the rescinding party fails in a “material” respect); Wyler v. Feuer, 85 Cal.App.3d 392, 403-404, 149 Cal. Rptr. 66, 633-634 (2d Dist. 1978) (“[c]ase law has uniformly held that a failure of consideration must be ‘material,’ or go to the ‘essence’ of the contract before rescission is appropriate.”).26 Limiting the scope of the substantive element of the validly issued opinion to those terms of the interests that are of the “essence” of the interests responds to this principle.

26 This principle also finds support in Delaware. See Loew’s Theatres, Inc. v. Commercial Credit Company, 243 A.2d 78, 81 (Del. Ch. 1968) (“... a charter provision which seeks to waive a statutory right or requirement is unenforceable”). In Loew’s Theatres, Commercial Credit defended its refusal to grant a shareholder list request by pointing to its 1912 Certificate of Incorporation permitting only shareholders holding in the aggregate 25% or more of its outstanding capital stock the right to inspect the corporation’s stock ledger, contrary to § 220 of the Delaware General Corporation Law, which grants that right to “any” stockholder for any proper purpose. While Loew’s Theatres was not a case addressing the valid issuance of stock, it demonstrates that one permissible remedy for an invalid charter restriction of statutory rights is for a court to ignore the restriction and grant the rights.
There was also considerable sentiment among the partnership and LLC practitioners who served on the CA Working Group that the substantive element of the validly issued opinion is a trap for the unwary and should not be subsumed in the validly issued opinion at all, but rather should be separately stated and negotiated with opinion recipients. To address this concern, the Alternative Entities Opinion Report recommends an alternative form of limitation to the validly issued opinion for opinion preparers who hold this view, as follows:

“Our opinion in paragraph _____ above confirms that the issuance of the Membership [LP] Interests satisfies the requirements of RULLCA [the LP Act] and the Company’s [LP’s] Articles of Organization [Certificate of Limited Partnership] and Operating [Limited Partnership] Agreement, including any necessary approvals by the manager[s] and members [general partner[s] and limited partners] of the Company and the receipt of the amount and kind of consideration, if any, required thereunder. The opinion does not address, and we express no opinion on, whether any of the provisions of the Operating [Limited Partnership] Agreement violate RULLCA [the LP Act] or the Articles of Organization [Certificate of Limited Partnership].”

Alternative Entities Opinions Report at 46.

This form of limitation would serve to highlight the issues addressed in this article, thereby focusing the attention of opinion preparers and recipients on the issues posed by the validly issued opinion. If the opinion recipient objects to the limitation, then the parties can address the issue with a view to reaching a satisfactory resolution of the scope of the opinion, as understood by both opinion giver and opinion recipient.

TriBar acknowledges the practice of providing a separate statement of the substantive element of the validly issued opinion in its Preferred Stock Opinions Report. As TriBar notes, some opinion recipients request that the substantive element of the duly authorized opinion be separately stated, and TriBar includes in its report one formulation opinion preparers sometimes use for this separate assurance:

“The rights, powers and preferences of the preferred stock set forth in the [charter] do not violate [the applicable corporation statute] or the [charter].”

TriBar Preferred Stock Opinions Report, 63 Bus. Law at 924.

For LLC and LP validly issued opinions, this “alternative” identified by TriBar might become the preferred form of the opinion. If so, then the validly issued opinion would be limited to the elements identified by TriBar (quoted under “The Scope of the Validly Issued Opinion for Alternative Entities” at the beginning of this article) but would not include the substantive element of the validly issued opinion: that element would be addressed in a separately stated opinion.

- James F. Fotenos
Greene Radovsky Maloney Share & Hennigh LLP
jfotenos@greeneradovsky.com

RECENT DEVELOPMENTS

Macquarie Decision Reversed On Appeal

In a recently issued brief opinion in Macquarie Capital (USA) Inc. v. Morrison & Foerster LLP, 2018 WL 326391 (N.Y. Sup. Ct. App. Div. January 9, 2018), the New York Supreme Court Appellate Division reversed the trial court’s dismissal of a complaint by an underwriter against its counsel for malpractice in
failing to bring to its attention information that would have caused the underwriter to refrain from underwriting a registered public offering by a Chinese company. The trial court had based its dismissal on a lack of proximate cause due to the underwriter’s being in possession of the same factual information as its counsel. The Appellate Division ruled that the trial court, rather than dismissing the case, should have determined whether the information, while admittedly in the underwriter’s possession, put the underwriter on notice without counsel’s interpretation. The Appellate Division quoted an earlier decision that a law firm may not shift to the client the legal responsibility it was specifically hired to undertake.

The case involved Macquarie’s acting as underwriter in a U.S. public offering for Puda Coal, Inc., which was described in the prospectus as conducting its major operations in China through a Chinese subsidiary. Macquarie retained Morrison as its counsel to assist, among other things, with due diligence. Macquarie also hired Kroll Inc. to conduct a factual investigation of publicly available information. Kroll issued a report that disclosed the existence of a public record indicating that Puda had transferred its interest in the subsidiary to its CEO and an institutional investor. Kroll provided the report to an associate at Macquarie, who emailed the report to other members of the Macquarie deal team and to Morrison with a cover email indicating “no red flags were identified.” Morrison later delivered a negative assurance letter to Macquarie stating that “nothing has come to our attention” that caused Morrison to believe that the offering documents contained false or misleading statements. When the fraud was discovered, Macquarie was sued by purchasers of the securities and separately by the SEC and eventually settled. Macquarie then sued Morrison.

The decision of the Appellate Division was procedural, addressing what was appropriate to decide on a motion to dismiss, and did not deal with the merits of whether Morrison’s failure to alert Macquarie to the problem was the proximate cause of Macquarie’s loss. Morrison may succeed in demonstrating that its client, an experienced underwriter, was in as good a position as it was to assess the significance of the information in the Kroll report regarding Puda’s transfer of interests in its subsidiary.

- Stanley Keller
  Locke Lord LLP
  stanley.keller@lockelord.com

LEGAL OPINION REPORTS

(See Chart of Published and Pending Reports on following page.)


Chart of Published and Pending Reports

[Editors’ Note: The chart of published and pending legal opinion reports below has been prepared by John Power, O’Melveny & Myers LLP, Los Angeles, and is current through December 31, 2017.]

A. Recently Published Reports

<table>
<thead>
<tr>
<th>ABA Business Law Section</th>
<th>2009</th>
<th>Effect of FIN 48 – Audit Responses Committee</th>
</tr>
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<tbody>
<tr>
<td></td>
<td></td>
<td>Negative Assurance – Securities Law Opinions Subcommittee</td>
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<tr>
<td></td>
<td>2010</td>
<td>Sample Stock Purchase Agreement Opinion – Mergers and Acquisitions Committee</td>
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<tr>
<td></td>
<td>2011</td>
<td>Diligence Memoranda – Task Force on Diligence Memoranda</td>
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<td></td>
<td>2013</td>
<td>Survey of Office Practices – Legal Opinions Committee</td>
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<td></td>
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<td>Legal Opinions in SEC Filings (Update) – Securities Law Opinions Subcommittee</td>
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<td></td>
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<td>Revised Handbook – Audit Responses Committee</td>
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<td></td>
<td>2014</td>
<td>Updates to Audit Response Letters – Audit Responses Committee</td>
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<td></td>
<td>2015</td>
<td>No Registration Opinions (Update) – Securities Law Opinions Subcommittee</td>
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<tr>
<td></td>
<td></td>
<td>Cross-Border Closing Opinions of U.S. Counsel</td>
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<tr>
<td></td>
<td>2016</td>
<td>Report on the Use of confirmation.com – Audit Responses Committee</td>
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<td>2017</td>
<td>Opinions on Debt Tender Offers — Securities Law Opinions Subcommittee</td>
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<table>
<thead>
<tr>
<th>ABA Real Property Section (and others)</th>
<th>2012</th>
<th>Real Estate Finance Opinion Report of 2012</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>2016</td>
<td>Local Counsel Opinion Letters in Real Estate Financing Transactions</td>
</tr>
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<table>
<thead>
<tr>
<th>Arizona</th>
<th>2004</th>
<th>Comprehensive Report</th>
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</table>

| California | 2007  | Remedies Opinion Report |
|            |      | Comprehensive Report |
|            | 2009  | Venture Capital Opinions |
|            | 2014  | Sample Venture Capital Financing Opinion |
|            | 2015  | Revised Sample Opinion |
|            | 2016  | Third-Party Closing Opinions: Limited Liability Companies and Partnerships |

29 These reports are available (or soon will be available) in the Legal Opinion Resource Center on the web site of the ABA Legal Opinions Committee, http://apps.americanbar.org/buslaw/tribar/. Reports marked with an asterisk have been added to this Chart since the publication of the Chart in the last quarterly issue of this Newsletter.

30 These Reports are the product of the Committee on Legal Opinions in Real Estate Transactions of the Section of Real Property, Trust and Estate Law, Attorneys’ Opinions Committee of the American College of Real Estate Lawyers, and the Opinions Committee of the American College of Mortgage Attorneys (collectively, the “Real Estate Opinions Committees”).
### Recently Published Reports (continued)

<table>
<thead>
<tr>
<th>State/Association</th>
<th>Year</th>
<th>Report/Update</th>
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<tbody>
<tr>
<td>Florida</td>
<td>2011</td>
<td>Comprehensive Report Update</td>
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<tr>
<td>Georgia</td>
<td>2009</td>
<td>Real Estate Secured Transactions Opinions Report</td>
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<tr>
<td>City of London</td>
<td>2011</td>
<td>Guide</td>
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<td>2017</td>
<td>Guide Update</td>
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<td>Maryland</td>
<td>2009</td>
<td>Update to Comprehensive Report</td>
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<tr>
<td>Michigan</td>
<td>2009</td>
<td>Statement</td>
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<td></td>
<td>2010</td>
<td>Report</td>
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<td>Multiple Bar Associations</td>
<td>2008</td>
<td>Customary Practice Statement</td>
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<td>Multiple Law Firms</td>
<td>2016</td>
<td>White Paper – Trust Indenture Act §316(b)</td>
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<td>National Association of Bond Lawyers</td>
<td>2011</td>
<td>Function and Professional Responsibilities of Bond Counsel</td>
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<tr>
<td></td>
<td>2013</td>
<td>Model Bond Opinion</td>
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<tr>
<td></td>
<td>2014</td>
<td>501(c)(3) Opinions</td>
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<td></td>
<td>2017</td>
<td>Update of Model Letter of Underwriters’ Counsel</td>
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<tr>
<td>National Venture Capital Association</td>
<td>2013</td>
<td>Model Legal Opinion</td>
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<td>New York</td>
<td>2009</td>
<td>Substantive Consolidation – Bar of the City of New York</td>
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<td>2012</td>
<td>Tax Opinions in Registered Offerings – New York State Bar Association Tax Section</td>
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<td>North Carolina</td>
<td>2009</td>
<td>Supplement to Comprehensive Report</td>
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<td>Pennsylvania</td>
<td>2007</td>
<td>Update</td>
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<td>South Carolina</td>
<td>2014</td>
<td>Comprehensive Report</td>
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<tr>
<td>Tennessee</td>
<td>2011</td>
<td>Report</td>
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<tr>
<td>Texas</td>
<td>2006</td>
<td>Supplement Regarding Opinions on Indemnification Provisions</td>
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<td></td>
<td>2009</td>
<td>Supplement Regarding ABA Principles and Guidelines</td>
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<tr>
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<td>2012</td>
<td>Supplement Regarding Entity Status, Power and Authority Opinions</td>
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<td></td>
<td>2013</td>
<td>Supplement Regarding Changes to Good Standing Procedures</td>
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</table>
Recently Published Reports (continued)

| TriBar        | 2008      | Preferred Stock |
|              | 2011      | Secondary Sales of Securities |
|              | 2011      | LLC Membership Interests |
|              | 2013      | Choice of Law |
|              | 2017      | Limited Partnership Opinions |

### B. Pending Reports

<table>
<thead>
<tr>
<th>ABA Business Law Section</th>
<th>Sample Asset Purchase Agreement Opinion – Merger and Acquisitions Committee</th>
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<tbody>
<tr>
<td></td>
<td>Updated Survey – Legal Opinions Committee</td>
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<td>Resale Opinions – Securities Law Opinions Subcommittee</td>
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<td></td>
<td>Opinions on Risk Retention Rules White Paper – Securitization and Structured Finance Committee &amp; Legal Opinions Committee</td>
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<table>
<thead>
<tr>
<th>ABA Real Property Section (and others)</th>
<th>UCC Opinions in Real Estate Transactions*</th>
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<tr>
<th>California</th>
<th>Sample Personal Property Security Interest Opinion</th>
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<tr>
<td></td>
<td>Exceptions and Other Qualifications to the Remedies Opinion</td>
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<tr>
<td></td>
<td>Sample Real Estate Finance Opinion</td>
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<td>Comprehensive Report Update</td>
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<th>Multiple Bar Associations</th>
<th>Statement of Opinion Practices</th>
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<tr>
<td></td>
<td>Core Opinion Principles</td>
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<td></td>
<td>Local Counsel Opinions(^{32})</td>
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<table>
<thead>
<tr>
<th>Florida</th>
<th>Comprehensive Report Update</th>
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<tr>
<th>Texas</th>
<th>Comprehensive Report Update</th>
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<tr>
<th>TriBar</th>
<th>Opinions on Clauses Shifting Risk</th>
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<td>Bring Down Opinions</td>
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<thead>
<tr>
<th>Washington</th>
<th>Comprehensive Report</th>
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\(^{31}\) See note 30.

\(^{32}\) A joint project of the ABA Legal Opinions Committee, the Working Group on Legal Opinions, and other bar groups.
MEMBERSHIP

If you are not a member of our Committee and would like to join, or you know someone who would like to join the Committee and receive our newsletter, please direct him or her here. If you have not visited the website lately, we recommend you do so. Our mission statement, prior newsletters, and opinion resource materials are posted there. For answers to any questions about membership, you should contact our membership chair Anna Mills at amills@vwlawfirm.com.

RECENT DEVELOPMENTS ON TWITTER

Kudos to the Committee’s Social Media Committee (Rick Frasch, Christina Houston, and Anna Mills) for establishing a Twitter account for Committee members and other interested students of opinion practice. Stay current on legal opinion developments @ABALegalOpinion. If you are a novice on Twitter, you can learn all about Twitter and join and follow Rick’s, Christina’s, and Anna’s tweets by going to the Internet and downloading a podcast at: https://www.howcast.com/videos/149055-how-to-use-twitter/.

33 The URL is http://apps.americanbar.org/dch/committee.cfm?com=CL510000.

NEXT NEWSLETTER

We expect the next newsletter to be circulated in April 2018. Please forward cases, news and items of interest to Ettore Santucci (esantucci@goodwinprocter.com), Jim Fotenos (jfotenos@greeneradovsky.com), or Susan Cooper Philpot (philpotsc@cooley.com)