

Opinions of Counsel in Real Estate Finance Transactions

Assumptions, Qualifications, Limitations and Factual Certificates That Reduce Risks for Opinion Givers

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Certificates That Reduce Risks for Opinion Givers

Presented by: Scott J. Stein, *Stein Law, PLC*





Scott J. Stein is a transactional attorney at Stein Law, PLC and represents and advises businesses and individuals in their commercial real estate sales, leases and developments and other types of corporate and business transactions.

Stein Law and **Arizona Legal Opinions** prepare attorney opinion letters in all commercial transactions, including those in which we advise a client on legal matters from start to finish or for out-of-state attorneys or clients whose real estate transaction requires representation in Arizona.

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Please visit www.arizonalegalopinions.com/ for more information.



Preparing commercial real estate finance opinions

- ▶ A. Range and scope of opinions
- ▶ B. Assumptions (and Qualifications)
- ▶ C. Limitations
- ▶ D. Use of the opinion letter

Range of Opinions

- ▶ Introduction
- ▶ 1. A lender in a secured real estate financing transaction will generally require an opinion of counsel from borrower's counsel.
- ▶ 2. Borrower's counsel provides an opinion of counsel letter in conjunction with its representation of the Borrower.
- ▶ 3. Lender's often provide forms (as a starting place)

Real Estate Financing Documents

- ▶ 3. A secured real estate financing transaction includes:
 - ▶ i. A promissory note demonstrating the sum of funds to be repaid;
 - ▶ ii. A loan agreement describing the loan being made, the terms and conditions and detailing the agreements included in the loan package.
 - ▶ iii. A mortgage or a deed of trust, indicating the amount of the loan and the describing the real property securing the loan

Loan Documents (continued)

- ▶ iv. An assignment of rents;
- ▶ v. An environmental indemnity agreement;
- ▶ vi. Guaranty;
- ▶ vii. Miscellaneous documents
 - 1. UCC-1 Financing Statement
 - 2. Closing Certificate

Others:

Lenders will sometimes request that Commitments or Terms Sheets, be included, but should generally be excluded

A. Range of Opinions

- ▶ 1. Borrower is a _____ (type of business entity), duly organized and validly existing and in good standing under the laws of the State of _____ (state where real property is located).
- ▶ 2. Each loan document has been properly authorized, executed, acknowledged and delivered by Borrower.

Range of Opinions (continued)

- ▶ 3. Each loan document constitutes the legal, valid and binding obligation of the Borrower, enforceable against the Borrower in accordance with its terms.
- ▶ 4. The choice of law of the State of _____ to govern the loan documents is legal, valid, binding and enforceable under the laws of such State.

Range of Opinions (continued)

- ▶ 5. The payment by the Borrower and receipt by the Lender of all principal and interest and other payments required to be paid pursuant to the terms of the Note and the other loan documents will not violate the usury laws of the State of _____ or otherwise constitute unlawful interest.
- ▶ 6. Borrower has all the requisite power and authority to execute and deliver each of the loan documents.

Range of Opinions (continued)

- ▶ 7. Borrower has the legal power and authority to borrow money and to own and encumber its property and assets located in _____, _____.
- ▶ 8. No order, consent, approval, license or authorization of, or filing, recording or registration with, any governmental or public body or authority of the United States is required in connection with the execution and delivery of the loan documents.

Range of Opinions (continued)

- ▶ 9. The execution and delivery of the loan documents and the performance of the terms and conditions contained in the loan documents will not conflict with, or constitute a default with any laws, statutes or regulations.

B. Assumptions

- ▶ 1. The actual intent of the borrower and the lender is accurately set forth in the loan documents.
- ▶ 2. All terms and conditions of, or relating to the transactions contemplated by the loan documents are correctly and completely embodied in the loan documents.

Assumptions (continued)

- ▶ 3. The Mortgage (Deed of Trust) will be properly recorded in the office of the County Recorder of _____ County, _____.
- ▶ 4. The consideration recited in the loan documents will be advanced pursuant to the terms of the loan documents.
- ▶ 5. All signatures not witnessed by us are genuine.

Assumptions (continued)

- ▶ 6. All documents submitted to us as originals are authentic.
- ▶ 7. All documents submitted to us as copies are accurate and complete copies of the originals thereof.
- ▶ 8. The loan documents and the transactions evidenced by the loan documents are valid, binding and enforceable with regard to lender.

Related Qualifications

- ▶ 1. The enforceability of the loan documents may be limited by statutory and case law pertaining to bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance, equitable subordination, marshaling, lender's fiduciary duty and lender's bad faith.
- ▶ 2. The enforceability of the loan documents may be limited by general principles of equity.

Related Qualifications (continued)

- ▶ 3. The enforceability of certain rights and remedies provided in the loan documents are limited or may be unavailable by certain laws and judicial opinions and decisions.
- ▶ 4. The enforceability of certain rights and remedies provided in the loan documents may be limited by public policy.

C. Limitations

- ▶ 1. We have not made or undertaken to make any investigation of the state of title to the real property described in the loan documents.
- ▶ 2. We express no opinion with respect to title thereto or the priority or perfection of any liens on the real property to any security interests.

Limitations (continued)

- ▶ 3. We are licensed to practice law only in the State of _____.
- ▶ 4. We express no opinion with respect to the effect of any laws other than the laws of the State of _____ and the laws of the United States of general application to transactions in the State of _____.

Limitations (continued)

5. We undertake no obligation to advise you of facts or changes in the law occurring after the date of this opinion letter which might affect the opinions expressed in this opinion letter.

D. Use of Opinion Letter

- ▶ 1. This opinion is being rendered for the benefit of lender and the benefit of lender's successors and assigns under the loan documents.
- ▶ 2. This opinion may not be used or relied upon by, nor may copies be delivered to, any other person or entity without our prior written consent.
- ▶ 3. The opinions set forth in this opinion letter are limited to the matters expressly stated in this opinion letter and no opinion is implied or may be inferred beyond the matters expressly so stated.
- ▶ Other Firms? If in connection with another opining firm/local counsel

POTENTIAL RISKS OF LIABILITY AND PROTECTIONS FOR OPINION PREPARER

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INTRODUCTION

1. Why are attorneys asked to provide opinions of counsel for business deals in general and for loan transactions secured by real estate?
2. It would seem that if loan documents were prepared by lender's attorneys:
 - i. The lender's attorneys would just as easily be able to opine on the enforceability of the loan documents;
 - ii. A preliminary title report and policy of title insurance would cover any claims against title, including but not limited to lawsuits that have or might have judgment liens against the property;
 - iii. A certificate from the state agency with jurisdiction over the borrower would provide evidence that the borrower is in good standing and authorized to do business.

3. Having borrower's counsel provide an opinion of counsel appears to be a form of risk-sharing in which the lender regards the borrower's counsel's policy of professional liability insurance as another source of a remedy in the event the loan fails.
4. This part of the seminar addresses the risks and liabilities faced borrower's counsel in providing an opinion of counsel for a loan transaction secured by a mortgage or deed of trust in real property as well as a security interest in personal property.

Duties of Opinion Giver

1. Some of the opinions that a borrower's counsel is asked to provide include, but are not limited to,
 - i. enforceability of the agreements;
 - ii. no liens or claims on title;
 - iii. borrower's good standing and authority to do business; and
 - iv. the agreements contemplated by the agreements will not cause a breach of the organizational documents or any other documents.

Duties of Opinion Giver

2. Other seminar materials discuss the necessities to limit the scope of the opinion to opinions by different forms of evidence (e.g., certificate of borrower, certificate of secretary of state; title insurance; environmental audit as well as to exceptions and restrictions provided by state and federal law.

Duties of Opinion Giver

3. In providing an opinion of counsel, an attorney (and his or her law firm) is held to general standards of care that may be owed to the attorney's own client. It may be inferred that a similar standard of care is owed to the lender or other recipient of the opinion of counsel.

Duties of Opinion Giver

3. Standard of Care. The Restatement of Law Governing Lawyers (American Law Institute 2006) discusses a lawyer's duty of care:

§51 Duty of Care to Certain Nonclients

For purposes of liability under §48, a lawyer owes a duty of care within the meaning of §52 in each of the following circumstance:

1...

Duties of Opinion Giver

2. To a nonclient when and to the extent that:
 - (a) The lawyer or (with the lawyer's acquiescence) the lawyer's client invites the nonclient to rely on the lawyer's opinion or provision of other legal services, and

The nonclient so relies; and

- (b) The nonclient is not, under applicable tort law, too remote from the lawyers to be entitled to protection;
3. To a nonclient when and to the extent that:
 - (a) The lawyer knows that a client intends as one of the primary objectives of the representation that the lawyer's services benefit the nonclient
 - (b) Such a duty would not significantly impair the lawyer's performance of obligations to the client

Duties of Opinion Giver

- I. Under New York law, an attorney representing a borrower may have liability to a lender in connection with an opinion letter issued in a loan transaction. *Prudential Insurance Company v. Dewey, Ballantine, Bushby, Palmer & Wood*, 80 N.Y.2d 377, 605 N.E.2nd 318, 590 N.Y.S. 831 (1992)

Duties of Opinion Giver

- II. The purpose of an opinion letter is to aid the lender in deciding whether to make the loan. *Fortress Credit Corp. v. Dechert LLP*, 89 A.D.3d 615, 934 N.Y.S.2d 119 (2011).

Duties of Opinion Giver

- III. To establish a duty owed by an attorney to a non-client the latter must allege and prove that the intent to benefit the non-client was a direct purpose of the transaction or relationship. *Flaherty v. Weinberg*, 303 MD 116, 492 A.2d (1985)

Duties of Opinion Giver (cont.)

4. Satisfaction of the diligence and competence standards requires “the competence and diligence normally exercised by lawyers in similar circumstance”. This in turn requires reference to customary practice.
 - I. In general, the opinion giver will satisfy its duty of care if it exercises the diligence and meets the competence standard that lawyers who regularly give opinions of the kind involved in similar transactions.
 - II. A closing opinion requires factual and legal diligence. Legal diligence means the process of considering how the law covered by the opinion applies to the contract in question.
 - III. Customary practice is a primary determinant of the nature and extent of the legal diligence required to be employed by the opinion giver in preparing and giving an opinion letter.

Duties of Opinion Giver (cont.)

5. One recommended procedure:

- I. One or more competent opinion preparers who are reasonably current in development in applicable law and practice read the entire relevant contracts carefully.
- II. If the opinion preparers recognize in the process of that review an issue giving rise to a significant degree of uncertainty as to the enforceability of a particular undertaking, then they determine whether the opinion would cover the issue giving rise to the uncertainty after considering the exclusionary effect of general exceptions, customary usage and other factors.
- III. If the opinion would cover the issue, the opinion preparers do what is reasonably necessary to satisfy themselves whether the undertaking is enforceable. This may include reliance on their knowledge of the law, consultation with other lawyers or legal research.
- IV. If the opinion preparers are still not satisfied that the undertaking is enforceable, then they include in the opinion letter an exception that expressly excludes or limits coverage of the doubtful provision.

Duties of Opinion Giver (cont.)

V. Borrower's Certificate

1. Attorney will prepare a borrower's certificate which will generally provide the basis for certain facts on which opinions are based:
 - i. Pending or actual litigation, bankruptcy;
 - ii. Existing documents being certified as true and correct;
 - iii. Obtained consents
 - iv. Known defects or representations
 - v. Execution of the loan documents will not result in a breach of the company's organizational documents

Misrepresentations/Mistakes

1. For a non-client to succeed in a negligence action against an attorney, it must prove that the primary purpose and intent of the attorney-client relationship was to benefit or influence the third party. *Greycas, Inc. v. Proud*, 826 F.2d 1560 (7th Cir. 1987).
2. Attorney who issued a misleading opinion letter may be liable to a non-client based on negligent misrepresentation. *Mehaffy, Rider, Windholz & Wilson v. Central Bank of Denver, N.A.*, 892 P.2d 230 (1995).

Misrepresentations/Mistakes

3. Rule 4.1 of the Model Rules of Conduct. In the course of representing a client a lawyer shall not knowingly:
 - (a) make a false statement of material fact or law to a third person; or
 - (b) fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by Rule 1.6.

Misrepresentations/Mistakes

4. Absent a misleading opinion, an opinion giver is not obligated to proceed beyond the opinion's scope, as it might for a client.
 - (a) Customary practice is to exercise reasonable professional judgment in identifying enforceability issues related to every undertaking in a contract.
 - (b) It does not call for knowledge or research of the law relating to every undertaking, except to the extent required by professional judgment.

Misrepresentations/Mistakes

5. This line of cases should not be interpreted as defining the duty of care to opinion recipients differently from customary practice.

Cost/Benefit Analysis

1. The basic question is whether the potential liability in an opinion of counsel outweighs the benefits.
2. The opinion recipient may view the opinion giver as an indemnifier of the transaction. An opinion may be covered by the policy of professional liability insurance. Alternatively, the opinion giver may seek indemnification from the client. (See, for instance, New York State Bar Association Op. 969, June 12, 2013).
3. The opinion recipient may view the opinion giver as liable for the entire loss and may seek to attach the insurance policy and personal liability of the individual attorney.
4. The opinion givers may incur defense costs that far exceed what they could afford to lose.

Cost/Benefit Analysis

5. The benefits include payment for legal services as well as continued representation of the client in future transactions.
6. It makes sense to limit financial exposure to a manageable and predictable amount.

Consequences

1. The cases discussed in this section of the seminar support the proposition that an attorney giving an opinion of counsel may be liable to a third party lender or other opinion recipient.
2. The duty of care owed to a third party is a duty of general care, satisfied by competence and diligence.