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DANGER AHEAD! LEGAL OPINIONS FOR COLORADO LAWYERS (A version of this paper is scheduled for publication in the April 2009 issue of *The Colorado Lawyer*)

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Legal opinions are easy to identify – whenever an attorney gives advice to a client, a legal opinion is usually offered. Not all opinions contain the word “opinion” or “opine”, and not all opinions are included in letters. Opinions may be given by e-mail, memorandum, casual correspondence, and other informal written and oral methods of communication and may, for example, include the following:

- We have completed your licensing activities in Tennessee and, therefore, you may now conduct your business in the state of Tennessee.
- We believe you have meritorious claims that can be pursued in litigation.

Formal opinion letters are usually required by agreement at the closing of a transaction to which the client is a party, and these are referred to as “closing opinions.” An example of opinions generally included in a closing opinion are the following:

It is our opinion that the company is duly incorporated and in good standing under the laws of the state of Colorado and the transaction documents are enforceable against the company.

Legal opinions offered and received by lawyers for governmental entities are frequently specialized opinion letters, received and given in the context of bond closings, leases, and lease-purchase arrangements, among other situations. To minimize the risk in offering and accepting legal opinions, Colorado lawyers must not only be well-versed in their client’s business and the

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attendant law, but also in custom and practice (also referred to as “customary practice”) as defined by the available literature regarding third-party legal opinions and the specific Colorado guidance on point. It is important to note that what may be considered customary in one situation (a real estate closing) may not be customary in other situations (such as a bond closing). Nevertheless, as discussed below in the case of *Mehaffy, Rider, Windholz & Wilson v. Central Bank Denver*,³ bond offerings can lead to opinion liability as in any other transaction. In litigation, a decision whether the opinion giver has satisfied its duty of care is determined by reference to the customary practice of “lawyers who regularly give and who regularly represent recipients of opinions of the kind involved”⁴ – and this is usually established by experts and references to bar association reports and treatises.

The purpose of this article is to discuss customary practice among attorneys experienced in giving and receiving third party opinion letters, to bring awareness to Colorado practitioners of the risks associated with giving third party legal opinions, and to discuss the limited amount of Colorado guidance available to opinion givers and recipients.

Customary Practice and Usage

Customary practice among lawyers is incorporated into closing opinions. The American Law Institute’s *Restatement (Third) of the Law Governing Lawyers*, Section 95 (Reporter’s *Note* to Comment c) states:

In giving ‘closing’ opinions, lawyers typically use custom and practice to provide abbreviated opinions that facilitate the closing. Such opinions may not recite certain assumptions, limitations, and standards of diligence because they are understood between counsel.

The Reporter’s *Note* adds that custom and practice covers the “meaning of the opinion letter including all such assumptions, limitations, and diligence standards.” Customary practice includes specific Colorado guidance and more broadly applicable national literature. Any attorney not familiar with customary practice and yet issuing or receiving a closing opinion in a business transaction is entering dangerous territory.

In 2008, the *Business Lawyer* published a *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions* (the “*Statement*”) adopted by

³ 892 P.2d 230 (Colo. 1995).

⁴ *Glazer and Fitzgibbon on Legal Opinions: Drafting, Interpreting, and Supporting Closing Opinions in Business Transactions* (Aspen Law & Business, 3rd Ed.) §1.6.1 at 30. See, also, *Restatement (Third) of the Law Governing Lawyers*, §52, Comment b.

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25 state bar association groups, the American College of Real Estate Lawyers and the American College of Mortgage Attorneys, among other groups.⁵ Citing the *Restatement*, the *Statement* provides that “[t]he role of customary practice in third-party legal opinion practice is well-established.” The *Statement* goes on to say, “[c]ustomary practice evolves to reflect changes in law and practice.” The one and one-half page *Statement* concludes that “customary practice applies” whether or not the opinion specifically “refer[s] to the application of customary practice.” When interpreting closing opinions, the recipient of the opinion and any court interpreting the opinion should recognize the importance of customary practice and not merely interpret the opinion within its four corners. ① ②

Colorado Guidance

The literature defines the meaning of terms used in a legal opinion, and sets forth the due diligence necessary to establish the foundation for the various legal opinions. The literature that defines customary practice is national and local, and extensive.⁶ Colorado, however, (unlike many other states) has not adopted its own opinion report setting forth an interpretation of customary practice in Colorado and has no specialized rules governing third-party legal opinion practice although there are two cases discussed below that address attorney liability for closing opinions.⁷

Colorado’s only specific rules on the subject are included in Colorado’s Rules of Professional Conduct, specifically:

- An attorney may undertake an evaluation of a matter affecting a client for use by a person other than the client if the attorney believes that such evaluation is consistent with his or her duties to the client, and if requested by the client (Rule 2.3);

⁵ *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions*, 63 The Bus. L. (ABA) 1277 (Aug. 2008). The *Statement* has been formally adopted by the Business Law Section of the Colorado Bar Association (November 2008) as well as the Real Estate Section of the Colorado Bar Association (February 2009).

⁶ See *Third-Party “Closing” Opinions*, 53 The Bus. L. (ABA) 591 (1998) (A Report of the TriBar Opinion Committee) (“1998 TriBar Report”) and *Guidelines for the Preparation of Closing Opinions*, 57 The Bus. L. (ABA) 875 (Feb. 2002)

⁷ See *Mehaffy, Rider, Windholz & Wilson v. Central Bank of Denver, N.A.*, 892 P.2d 230 (Colo. 1995) and *Zimmerman v. Dan Kamphausen Co.*, 971 P.2d 236 (Colo. App. 1998).

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- The lawyer must be competent in the facts, law, and customary practice to render the opinion or, when representing the opinion recipient, competent to advise the client as to the meaning and effect of the opinion (Rule 1.1; customary practice is incorporated into Rule 1.1 through the *Restatement (Third) of the Law Governing Lawyers*, Section 95 as well as the standards in the community for opinion givers and recipients);
- The lawyer must preserve the confidentiality of client information and only make disclosure of confidential information with client consent (Rule 1.6); and
- The lawyer's conduct must conform to the requirements of the law and must be characterized by independent judgment and truthfulness in statements to others (Rules 1.2, 2.1 and 4.1).

Other Literature and Other Jurisdictions

There is a significant amount of literature available from other jurisdictions and the American Bar Association setting forth views on customary practice. This literature is easily available and much of it can be found in the ABA's legal opinion resource center.⁸ Of these, the ABA's "Guidelines for the Preparation of Closing Opinions"⁹ and "Legal Opinion Principles"¹⁰ are among the most significant, as are the reports prepared by the TriBar Opinion Committee.¹¹ The TriBar Opinion Committee has been publishing reports about legal opinions and customary practice since 1979.¹² The *1998 TriBar Report*¹³ contains an extensive discussion of customary practice relating to giving and receiving legal opinions.

⁸ <http://www.abanet.org/buslaw/tribar/home.shtml>. The website of the American College of Real Estate Lawyers (www.acrel.org) includes valuable information for persons writing legal opinions in real estate transactions. There are also numerous treatises available, including contributions from a number of Colorado lawyers in Holderness and Wunnicke, *Legal Opinion Letters Form Book* (Aspen Law Business, 2nd Ed. 2003). Chapter 1B of the 2008 Supplement is an excellent primer for lawyers not experienced in opinion practice. *Glazer and Fitzgibbon on Legal Opinions: Drafting, Interpreting, and Supporting Closing Opinions in Business Transactions* (Aspen Law & Business, 3rd Ed.) is another valuable resource for legal opinion preparers.

⁹ 57 The Bus. L. (ABA) 875 (2002).

¹⁰ 53 The Bus. L. (ABA) 831 (1998).

¹¹ The TriBar Opinion Committee was initially established by the New York County Bar Association, the Association of the Bar of the City of New York, and the New York State Bar Association. It now includes members throughout the United States.

¹² *Legal Opinions to Third Parties: An Easier Path*, 34 The Bus. L. (ABA) 1891 (1979).

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Notwithstanding the breadth of the literature, the definitions of “customary practice” are incomplete. “Customary practice permits an opinion giver and an opinion recipient . . . to have common understandings about an opinion without spelling them out. . . . By providing content to abbreviated opinion language, customary practice permits the omission from an opinion letter of the descriptions of the procedures that the opinion giver has performed and of many definitions, assumptions, limitations, and expectations.”¹⁴ The *1998 TriBar Report*¹⁵ defines “custom and practice” as having two components, (i) custom and usage and (ii) custom and diligence:

Custom and usage means that, in legal opinions, certain words and phrases expressing legal concepts have special meanings in the context of specific legal opinions – and the meaning may not be consistent with the dictionary definitions. For example, the phrase “legal, valid, binding and enforceable,” when used in the context of a remedies opinion (such as in the opinion “The agreement is legal, valid, binding and enforceable.”), has the same meaning as “enforceable” by itself.

Custom and diligence describes the extent of factual and legal due diligence that an attorney, giving an opinion, is expected to undertake to support an opinion. Opinion letters often state that the opinions given are based on a review of specific documents “and such other investigation as we [the opinion giver] has deemed appropriate.” Whether stated or not, custom and practice requires that the opinion giver perform the required legal and factual investigation.

Unfortunately that is about as clear as “custom and practice” or “customary practice” gets. The practical application of customary practice is discussed throughout the remainder of this article.

Negotiate The Opinion Early In The Transaction and Opinion Review

Where a lender or other third party is going to require a legal opinion at the closing of the transaction, customary practice suggests that the requirement be announced early in the transaction and that the opinion giver and the opinion recipient negotiate the opinion as early as possible, in many cases even before the negotiations for the transaction documents are

¹³ 1998 TriBar Report.

¹⁴ *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions*, 63 The Bus. L. (ABA) 1277 (Aug. 2008).

¹⁵ 1998 TriBar Report at § 1.4.

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completed. When opinions are left to the end of the transaction to negotiate, a very uncomfortable situation can develop for the attorney giving the opinion in that the client may blame the attorney for delaying the closing. If the opinion giver does not negotiate the difficult issues in the opinion early enough in the transaction, the opinion giver may be caught between holding up the transaction or assuming the liability for an inappropriate opinion or performing inadequate due diligence.

Customary practice also suggests that attorneys giving an opinion consult with other attorneys before the opinion is rendered. This may be through the law firm's formal opinion committee or on an *ad hoc* basis with a partner or colleague.¹⁶

Establishing Facts

Factual Certificates

A legal opinion involves application of law to facts. Customary practice contemplates that opinion givers will establish facts necessary for the legal opinion in a number of ways, including public official certificates, review of contracts and agreements, attendance at board and committee meetings, and factual certificates received from corporate officers. The *1998 TriBar Report* notes that the individual should execute any certificate making factual representations as an individual, and not on behalf of the company, explaining: "This practice is followed because a certificate by the Company would merely restate a Company representation made in the agreement or another transaction document. By signing as an individual, the officer takes personal responsibility for the representations made in the certificate."¹⁷

In performing due diligence, customary practice provides that an opinion giver is entitled to rely on factual information provided by an appropriate source if the opinion giver does not know the information to be untrue, the information does not appear to be irregular on its face, and the opinion giver does not know of circumstances that would make reliance to be unwarranted.¹⁸ Customary practice does not permit opinion givers to rely on unreliable factual information or in other circumstances where reliance would be unreasonable. In addition,

¹⁶ *Law Office Opinion Practices*, 60 *The Bus. L. (ABA)* 327 (2004) (Analysis of a Survey by the Committee on Legal Opinions, ABA Section of Business Law).

¹⁷ 1998 TriBar Report at § 2.5.4.

¹⁸ See Restatement (Third) of the Law Governing Lawyers, §95, com. c; Legal Opinion Principles (ABA) §III.A; 1998 TriBar Report at §2.1.4 and n. 41. See, also, *Glazer and Fitzgibbon on Legal Opinions: Drafting, Interpreting, and Supporting Closing Opinions in Business Transactions* (Aspen Law & Business, 3rd Ed.), Chapter 4, *Establishing the Factual Basis for the Opinion*.

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opinion givers may not rely on “ultimate facts” – statements that are tantamount to legal opinions themselves.¹⁹ For example, the opinion giver cannot rely on an officer’s certificate that says: “There are no breaches of [a specified agreement].” An opinion giver may rely on an officer’s certificate that says: “The undersigned is not aware of any facts or circumstances that might give rise to an allegation of breach of [the contract] and no person has given notice of any alleged breach of [the contract].”

Factual Assumptions

A factual assumption can be used where information necessary to establish required facts is not available, the facts being assumed relate to parties other than the client, and where the cost required to establish such facts exceeds the anticipated benefit. While some assumptions are so common to transactions that they may not be described in the legal opinion, other assumptions should be specifically stated. However, determining whether to specifically state factual assumptions is a difficult question, and most opinion givers overstate rather than understate factual assumptions.

Generally customary practice allows the opinion giver to assume that the signatories to the transaction documents are competent and adults. Another factual assumption accepted in customary practice is that the other (non-client) signatories to the transaction documents have executed the agreement with all necessary authority and capacity and, as a result, the transaction documents are enforceable against all other parties. Even though accepted in customary practice, these assumptions are frequently expressly stated in the opinions.

It is not unusual for an attorney, in performing due diligence for an opinion, to find that there are gaps in corporate minutes or records. These gaps could be relating to an amendment to the corporation’s articles of incorporation or the issuance of some shares. Where the missing minutes are not recent, corporate procedures indicate that formalities were followed, and the subsequent records indicate that that matters in question were treated as having occurred, customary practice suggests that the opinion giver is entitled to rely on the presumption of regularity and continuity in the corporate records without disclosure to the opinion recipient.²⁰

The Remedies Opinion and its Exceptions

The remedies opinion – that the agreement is enforceable (or “legal, valid, binding and enforceable”) – is frequently the most significant opinion given. It is the opinion that the

¹⁹ 1998 TriBar Report at § 2.2.1(b).

²⁰ 1998 TriBar Report at § 2.4.

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recipient wants most to receive and is generally the reason that opinions are requested. Customary practice provides that the remedies opinion offers the opinion that each and every provision of the contract providing a remedy is enforceable – unless specifically excluded.²¹ As a matter of customary practice, an opinion on the enforceability of an agreement is understood to mean that:

- (i) An agreement has been formed;
- (ii) Remedies provided by the agreement will be given effect by the courts; and
- (iii) The opinion describes the extent to which the courts will enforce the provisions of the agreement that are unrelated to the concept of breach.

To the extent there are any exceptions to the remedies opinion, they must be stated in the opinion.

Laws Included in the Remedies Opinion

A remedies opinion is generally understood to include coverage of contract, usury,²² general corporate, employment and intellectual property laws unless specifically excepted. Usury reflects a significant difficulty for an opinion giver, because it requires a conclusion not only as to the law, but also to a mathematical calculation of the interest rate, a calculation that may be difficult (if not impossible) where “interest” includes not only traditional interest, origination fees, and lender reimbursement, but also elements of equity participation such as common stock, common stock purchase warrants, or a profits interest in the business. In Colorado, where an obligation has a higher interest rate than is permitted by law, the obligation will be invalid to the extent that the interest rate is usurious, but it will still be enforced at the maximum allowable rate. Consequently, where a usurious interest rate is involved, a debt instrument will not be “enforceable”.²³ It may be substantially easier, and usually acceptable to the lender, to except usury from the remedies opinion – but the exception must be specifically stated.

Where a specific law is an issue to the transaction or the opinion recipient, it should be specifically addressed. It is always fair to ask that a legal opinion specifically cover laws potentially applicable to the transaction – but it is not fair to assume that the opinion covers them

²¹ 1998 TriBar Report at §§ 3.1 and 3.2.

²² 1998 TriBar Report at § 3.1.

²³ Colorado law discusses usury in C.R.S. § 5-12-103 and criminal usury in C.R.S. § 18-15-104.

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unless specifically stated. Unlike questions of usury in a loan transaction and certain other laws,²⁴ customary practice has not evolved to include or exclude the USA PATRIOT Act and other money-laundering laws, trading with the enemy laws, anti-terrorism laws, foreign asset control and sanctions laws, and other such legal considerations; therefore, a clear statement to the appropriate effect should be included in the opinion letter to avoid confusion and later dispute.

Exceptions to the Remedies Opinion

There are many potential exceptions to the remedies opinion. Bankruptcy and equitable principles are commonly permitted as exceptions, and are understood by customary practice to apply to all remedies opinions whether or not expressly stated in the opinion.²⁵ When stated, the exception is generally as follows: “The contract is enforceable, except as may be limited by bankruptcy, insolvency, or other similar laws affecting the rights and remedies of creditors generally and general principles of equity.”

Many other exceptions can be included where appropriate to the remedies opinion, including an exception to enforceability to the extent the funding for the contractual arrangement violates the USA PATRIOT Act,²⁶ for example. Many transaction documents include indemnification agreements, and most closing opinions will specifically except indemnification provisions from the enforceability provision.²⁷ Similarly pre-dispute waivers of jury trial may be included in many agreements but will generally be subject to an exception from the enforceability opinion because at least one state (California) has held such waivers to be unenforceable.²⁸ The U.S. Supreme Court recently held that an arbitration agreement that

²⁴ See 1998 TriBar Report at § 3.1.

²⁵ Section 3.3.1 of the 1998 TriBar Report and footnote 22 to the Boston Bar Association’s *Streamlined Form of Closing Opinion* (September 20, 2005) note that, even though understood by customary practice to apply to remedies opinions, these exceptions are usually expressly stated.

²⁶ “Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001” (Pub.L. 107-56).

²⁷ See generally 1998 TriBar Report at § 3.2; *Accord* at § 14. Note that in securities matters, Item 510 of Regulation S-K describes the Securities and Exchange Commission’s position on indemnification – that it is against public policy “and therefore unenforceable.”

²⁸ See *Grafton v. Superior Court*, 36 Cal.4th 944, 116 P.3d 479 (Calif. Sup. Ct. 2005). While this was a California decision based on the California Constitution, other states where the issue has not been addressed may find the reasoning to be instructive.

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provided for judicial review that went beyond the review provided for in the Federal Arbitration Act (“FAA”) was unenforceable.²⁹

Although customary practice assumes that certain exceptions are included whether or not stated, there is no list of such exceptions. Thus, the common practice among many attorneys is to state within the closing opinion the desired exceptions to enforceability and the other opinions given.³⁰ On the other hand, a specific statement of exceptions should not, by its breadth or length, exclude other unstated exceptions to the extent they can be established by customary practice.³¹

Practical Realization and Material Default Comfort Provisions

“Practical realization” is a further limitation on the remedies opinion, but one with benefit to the opinion recipient. This is frequently used in real estate transactions when the transaction documents contain numerous specific remedies for breach of the agreement, but which may be inconsistent or even unenforceable as written. In giving a practical realization qualification, the opinion gives avoid the time and cost necessary to analyze each of the many remedies and to further analyze the inter-relationship among the various provisions. One example of a practical realization opinion is as follows:

Certain of the provisions of the Agreement may be further limited or rendered unenforceable by applicable law, but in our opinion such law does not make the remedies afforded by the Agreement inadequate for the practical realization of the principal benefits intended to be provided.

When “practical realization” is offered in an opinion, the remedies opinion should be understood to mean that, where inconsistent or legally defective remedies are set forth in an

²⁹ *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396 (2008). Interestingly, five months after the U.S. Supreme Court decision in *Hall Street*, the California Supreme Court reached the opposite decision under California’s arbitration statute, California Code of Civil Procedure §§ 1280-1298.8, holding “The California rule is that the parties may obtain judicial review of the merits by express agreement.” *Cable Connection, Inc. v. DIRECTV, Inc.*, 44 Cal. 4th 1334, 82 Cal. Rptr. 3d 229, 233 (2008).

³⁰ Specifically stating all exceptions can be avoided where the closing opinion incorporates the *Legal Opinion Accord*, included in the *Third Party Legal Opinion Report* of the Section of Business Law, American Bar Association (1991) (the “*Accord*”), 47 The Bus. L. (ABA) 167 (Nov. 1991). Few opinion recipients are willing to accept *Accord* opinions, primarily because of the perceived complexity of the *Accord*. Because of its age, the *Accord* list of exceptions is now incomplete.

³¹ See *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions*, 63 The Bus. L. (ABA) 1277 (Aug. 2008).

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agreement, the remedies provisions (taken as a whole) will provide the opinion recipient the benefits of its bargain following a breach by the opinion giver's client.

As an alternative to the practical realization qualification, the *New York Report*³² suggests the use of a "material default comfort" provision which is intended to avoid the "ambiguity inherent in the practical realization approach."³³ The *New York Report* provides a form of "material default comfort" provision as follows:

In addition, we advise you that certain provisions of the Loan Documents may be further limited or rendered unenforceable by applicable law, but in our opinion such law does not render the Loan Documents invalid as a whole or substantially interfere with the realization of the principal benefits and/or security provided thereby.³⁴

Both the practical realization qualification and the material default comfort provision recognize that the core of an opinion on a secured real estate transaction is the need for the creditor to be able to foreclose on the collateral to collect principal and interest following a default. The opinion with the practical realization qualification or a material default comfort provision provides this comfort to the opinion recipient. Anything beyond this should be specifically requested.³⁵

Inappropriate Opinion Requests and Factual Confirmations

The ABA's "Guidelines for the Preparation of Legal Opinions" sets forth the "Golden Rule" of opinion giving:

Don't ask for an opinion that you would be unwilling to give. Don't refuse to give an opinion that you would ask for.³⁶

³² Ass'n of the Bar of the City of New York, Comm. Of Real Prop. Law, Subcomm. On Mortgage Loan Opinions, and New York State Bar Ass'n, Real Prop. Section, Attorney Opinion Letters Comm., *Mortgage Loan Opinion Report*, 54 The Bus. L. (ABA) 119 (1998).

³³ The New York Report, 54 The Bus. L. (ABA) at 129 n. 39.

³⁴ The New York Report, 54 The Bus. L. (ABA) at 129.

³⁵ See, generally, Ezell, et al., *The Remedies Opinion and Custom and Diligence – the Real Estate Secured Transaction Approach: Is It Consistent with Custom and Non-Real Estate Legal Opinion Practice?*, 48 Real Property, Trust and Estate Law Journal (ABA) 1 (Spring 2008).

³⁶ *Guidelines for the Preparation of Closing Opinions* § 3.1 states the Golden Rule of opinion giving more eloquently:

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Notwithstanding the Golden Rule, requested opinions frequently contain inappropriate opinion requests and experience shows that this is a primary reason that opinions must be negotiated early in the transaction. Opinions as to “foreign qualification in all jurisdictions where the nature of the client’s business requires such qualification,” that all outstanding equity securities are “legally and validly issued, fully-paid and non-assessable,” and comprehensive contractual compliance are generally considered to be inappropriate opinions, at least in part because of the potential time burden on the opinion giver to perform the necessary due diligence on the opinion in relation to the value of the opinion to the opinion recipient.³⁷

Opinion recipients frequently request that the opinion giver offer factual statements. The most important part about such requests is that the opinion giver recognizes these requests for their purpose – they are a request for a factual confirmation; they are not a request for a legal opinion. For example:

- The company is not a party to any material litigation.
- The company has 1,000,000 shares of its common stock outstanding.
- The agreements contain no misstatement of material fact or omission to state a fact necessary, in light of the circumstances, to make the other facts stated therein not to be misleading.

In none of those cases is an attorney being asked to apply his or her legal judgment to a set of facts. The attorney is simply being asked to confirm facts. On the other hand, from the opinion recipient’s point of view, the information that counsel to the company has can be important, and the opinion recipient will frequently require these factual confirmations. When given, factual confirmations:

An opinion giver should not be asked to render an opinion that counsel for an opinion recipient would not render if it were the opinion giver and possessed the requisite expertise. Similarly, an opinion giver should not refuse to render an opinion that lawyers experienced in the matters under consideration would commonly render in comparable situations, assuming that the opinion is otherwise consistent with these Guidelines and the opinion giver has the requisite expertise and in its professional judgment is able to render the opinion. Opinion givers and counsel for opinion recipients should be guided by a sense of professionalism and not treat opinions simply as if they were terms in a business negotiation.

³⁷ ABA’s “*Guidelines for the Preparation of Closing Opinions*” at §§ 4.1, 4.2 and 4.3. There may be circumstances when an “inappropriate opinion request” is appropriate. For example, where there is a newly-formed entity, it may be appropriate to request an opinion as to the legality of the outstanding equity interests if that is important to the transaction. All opinion requests should be considered on a case-by-case basis.

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- should be set apart from the opinions (since they are not opinions);
- should be stated to be factual confirmations (which they are); and
- in most cases, should be qualified by the attorney's knowledge.

Where the attorney is a member of a large firm, customary practice provides that the attorney need not query every lawyer in the firm to determine whether he or she has any relevant knowledge, but merely those attorneys known to be regularly working for that client.³⁸ Note that a knowledge qualification does not limit the diligence required by customary practice.³⁹

Closing Opinion Liability

It is important to discuss the risks of liability associated with opinion practice. To do so, a starting place is "*Courting the Suicide King; Closing Opinions and Lawyer Liability*."⁴⁰ This article discusses the children's card game where the player loses when she draws the King of Hearts – the king holding a sword to his head. Similarly with closing opinions. The problem in the closing legal opinion practice is that you have to bet your net worth and ultimately, if not sufficiently careful, you will lose. As the article states, "The knowledge that someone is struck by lightning every year does not keep golfers off the golf course. Although the consequences are dire, the perceived risk is too small. Similarly, the knowledge that lawyers are now sued on opinions and that the damages sought can be catastrophic has not kept lawyers who work on financial transactions from giving third-party legal opinions."⁴¹

Even opinions that are wholly accurate can lead to potential liability. The ABA's Guidelines specifically state that the opinion giver should not give an opinion, although accurate in itself, which may, in the context given, mislead the recipient.⁴² Rule 1.2(d) of the Colorado Rules of Professional Conduct (identical to the ABA's Model Rules) provides similarly that "[a]

³⁸ See 1998 TriBar Report at § 2.2.2(a).

³⁹ See 1998 TriBar Report at § 2.6.1.

⁴⁰ Glazer and Lipson, "*Courting the Suicide King; Closing Opinions and Lawyer Liability*," Business Law Today (ABA) March/April 2008 avail. at <http://www.abanet.org/buslaw/blt/2008-03-04/lipson.shtml>.

⁴¹ Cases in which attorneys have either avoided liability or been found liable for their closing opinions are discussed below.

⁴² ABA's "Guidelines for the Preparation of Closing Opinions" at § 1.5.

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lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent” Colorado Rule 1.0(f) provides that the attorney’s knowledge “can be inferred from the circumstances.” Thus attorneys providing legal opinions must always be alert to the intended use of the opinion. Federal securities laws may impose liability where the offer or sale of securities by means of fraud includes a legal opinion, even where the opinion is wholly accurate.⁴³

Colorado Litigation

Colorado courts have twice addressed whether attorneys can be held liable for legal opinions delivered to non-client third parties. Both cases have concluded that lawyers can be held liable to non-clients for negligent misrepresentation when delivering an opinion on which the non-client relied.

In *Mehaffy, Rider, Windholz & Wilson v. Central Bank Denver*,⁴⁴ the non-client bank’s claims against the attorneys were predicated on opinion letters the attorneys had prepared in connection with the offer and sale of notes and bonds issued by the Winter Park development authority in which they opined that “the Town and the Authority have adopted the Urban Renewal Plan in accordance with requirements of the laws of the State of Colorado” and “insofar as the said litigation questions the adoption of the Urban Renewal Plan is a ‘blighted area,’ such allegations are without merit.”⁴⁵ The Court held that attorneys are subject to liability to non-

⁴³ Rule 10b-5(c) (17 CFR §240.10b-5) provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, . . . To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Rule 10b-5(c) has been used to hold lawyers responsible as primary actors where lawyers have given proper opinions in circumstances where they know or should know that the opinion will be used in the course of a fraudulent transaction. See the discussion of the *National Student Marketing* case at n. 42 and the *Enron* case at n. 43-44, below. In *Thompson v. Paul*, 547 F.3d 1055, 2008 WL 4693748 (9th Cir. 2008), the Ninth Circuit surveyed case law from the Third, Fifth, Sixth, and Seventh Circuits seeking to hold attorneys civilly liable for actions of their client in the context of securities representation. The Ninth Circuit found that a clear rule emerges to hold an attorney liable as a primary participant:

An attorney who undertakes to make representations to prospective purchasers of securities is under an obligation, imposed by Section 10(b), to tell the truth about those securities. That he or she may have an attorney-client relationship with the seller of the securities is irrelevant under Section 10(b).

⁴⁴ 892 P.2d 230 (Colo. 1995).

⁴⁵ *Id.* at 237-8:

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client third parties for negligent misrepresentation when an attorney “issues an opinion letter that contains material misstatements of fact when the opinion is issued on behalf of a client for the purpose of inducing a non-client to enter into a transaction.”⁴⁶ In reaching this conclusion, the Court held:

- In a claim for negligent misrepresentation, the misrepresentation must be of a material fact that presently exists or has existed in the past, and must not consist of a promise relating to future events without a present intention to fulfill that promise or an expression of opinion, neither of which can support a claim for negligent misrepresentation.⁴⁷
- In offering the legal opinions issued, the attorneys made “statements that may constitute statements of fact, not merely representations of law.”⁴⁸
- Reliance is a necessary element of a claim for negligent misrepresentation. Even though the opinion letter disclaimed the non-client bank’s reliance and the bank represented that it had conducted its own investigation into the issue, the Court found a material issue of fact existing as to reliance to preclude the requested summary judgment.⁴⁹
- There was no attorney-client relationship between the law firm and the bank and, therefore, the bank’s legal malpractice claim was properly dismissed.⁵⁰

In *Zimmerman v. Dan Kamphausen Co.*,⁵¹ a Denver law firm had issued an opinion to a creditor opining that the partnership was properly constituted, the partnership had the legal power to execute a guaranty of an underlying promissory note and to perform its obligations

⁴⁶ *Id.* at 235.

⁴⁷ *Id.* at 237. Citations omitted. The dissent disagreed with the majority’s finding that the opinions given were “mixed statements of fact and law,” and would have held that the attorneys’ opinions, which were clearly described as “opinion” in the letters, were just that. *Id.* at 244-5.

⁴⁸ *Id.* at 238.

⁴⁹ *Id.* at 238-9.

⁵⁰ *Id.* at 239.

⁵¹ 971 P.2d 236 (Colo. App. 1998).

under the guaranty, and the father (who executed the guaranty) was authorized to sign the guaranty on behalf of the partnership.

When the note went into default, the creditor sued the partnership and the other general partner (the son). The son claimed that the guaranty was outside of the scope of the partnership agreement and, therefore, unauthorized and that the father did not have the authority to bind the partnership. Both defenses clearly implicated the attorneys' opinions. Citing *Mehaffy*, the Court of Appeals reversed the trial court's grant of summary judgment finding that "the trial court erred in granting summary judgment in favor of the law firm and [partner] on plaintiff's claim of negligent misrepresentation." Addressing the attorneys' arguments that the letter set forth opinions of law (which could not be the basis for a negligent misrepresentation claim), the Court of Appeals stated:

. . . we do not read the law firm's opinion letter as representing only a series of legal opinions as distinguished from representations of fact. . . . Plaintiff's assertions that he relied on the letter's representation concerning the scope of the partnership's authority and that such reliance was to his detriment create issues of material fact on plaintiff's claim of negligent misrepresentation, and thus, the trial court erred in entering summary judgment on this issue.⁵²

Thus, both *Mehaffy* and *Zimmerman* determined that attorneys' opinions which are based on the attorneys' application of facts to the law can themselves be facts forming the basis for a negligent misrepresentation claim. Both *Mehaffy* and *Zimmerman* also found that, since there was no attorney-client relationship between the attorneys and the opinion recipient, there could not be any liability to the third-party opinion recipient for general negligence or malpractice.⁵³

The lessons for Colorado lawyers from the *Mehaffy* and *Zimmerman* cases are several:

- Each opinion letter should clearly distinguish legal opinions from factual representations, and perhaps include a self-serving statement that such legal opinions "are opinions only, not representations of fact."⁵⁴

⁵² *Id.* at 240.

⁵³ *Mehaffy*, 892 P.2d at 239; *Zimmerman*, 971 P.2d at 240.

⁵⁴ A disclaimer used to address the issues raised in the *Mehaffy* and *Zimmerman* cases is as follows: "The opinions herein are provided as legal opinions only, effective as of the date of this letter, and not as representations of fact. We understand that the addressee has made such independent investigations of the facts as the addressee deemed necessary, and that the determination of the extent of those investigations of fact that are necessary has been made independent of this opinion letter."

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- Factual representations should be qualified (where appropriate) by knowledge.
- Factual underpinnings for legal opinions should be specifically stated.

Other Jurisdictions

Liability stemming from legal opinions has been litigated in several other jurisdictions. In addition to federal securities law claims, state law claims of negligent misrepresentation, fraud and legal malpractice, among others, may be involved. The following sets forth some examples of litigated cases involving legal opinions.

In *SEC v. National Student Marketing Corp.*,⁵⁵ the court found that the attorney who rendered an opinion at the closing of a merger transaction knowing that the proxy solicitation had been based on a materially misleading proxy statement, had aided and abetted a Rule 10b-5 violation by the client.

Business Week magazine⁵⁶ reported that court-appointed bankruptcy examiner, Neal Batson, said that the opinion letters from Enron's counsel, Vinson & Elkins, LLP, were "crucial to Enron's ability to complete" complex "total return swaps" where Enron, in reality, retained control of the assets. At the time, Vinson & Elkins expressed concern about the opinions, stating in one memo, "We [are] unsure of how [the] opinion rendered satisfies the requirements of FASB." Vinson & Elkins partners knew that Enron's CFO, Andrew Fastow, controlled some of the purchasers. In his Final Report to the Bankruptcy Court, Mr. Batson criticized Vinson & Elkins for "a true sale" opinion delivered in connection with a transaction for which a valid business purpose was essential, even though Vinson & Elkins allegedly knew that there was no

⁵⁵ 457 F.Supp. 682 (D.D.C. 1978).

⁵⁶ "Enron's Last Mystery," available at http://www.businessweek.com/magazine/content/06_24/b3988056.htm. The subtitle to this article describes the content: "Was Enron's law firm, Vinson & Elkins, as blind to the company's shenanigans as it maintains? Internal messages reviewed by *BusinessWeek* suggest the firm doubted the legitimacy of some of Enron's business practices."

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valid business purpose for the transaction.⁵⁷ Ultimately Vinson & Elkins settled related litigation, agreeing in June 2006 to pay \$30 million to Enron's bankruptcy estate.⁵⁸

In *In re National Century Financial Enterprises, Inc. Investment Litigation*,⁵⁹ an investor, alleging information he was given in a private placement of securities was false and misleading, sued both the issuer on claims of violation of Rule 10b-5 and state blue sky laws and the issuer's attorneys on claims of fraud, negligent misrepresentation, aiding and abetting, conspiracy and primary violation of the state's blue sky laws arising from the opinion letter issued by the attorneys in the transaction. The opinion letter expressly incorporated the *Legal Opinion Accord*.⁶⁰ The court cited § 16 of the *Accord* which (consistent with customary practice) provides that unless explicitly addressed, the opinion letter does not address federal or state securities laws. The court found that, even if the *Accord* were not applied, the 'no violation of law' provision in the opinion letter did not encompass the alleged blue sky law violation. The court concluded that the opinion letter did not warrant that the offering documents would not contain material misrepresentations or omissions of fact and dismissed the claims against the law firm.

In *Dean Foods Company v. Pappathanasi*,⁶¹ counsel issued a "no litigation" confirmation to the opinion recipient at a transaction closing, which confirmation proved to be wrong. Dean Foods, who was represented by the defendant law firm, was a witness in a federal grand jury investigation of one of its customers. At the time of the transaction closing, the law firm had not had any contact regarding the investigation for approximately six months. Nonetheless, the law firm advised Dean Foods to disclose the investigation in the sale of its stock, but Dean Foods was concerned disclosure would cause complications with its shareholders. Based at least in part on the length of time since the law firm had last been contacted regarding the investigation, the attorney handling the investigation indicated it was his best "guesstimate" that the investigation had been closed. Without any inquiry to any third party as to the status of the investigation, the

⁵⁷ *In re Enron Corp.*, report of Neal Batson, Court-appointed examiner in the United States Bankruptcy Court for the Southern District of New York (Case no. 01-16034 (AJG)) Final Report (Nov. 4, 2003) at pages 48-55, summary available at http://www.calbar.ca.gov/calbar/pdfs/sections/buslaw/opinions/2005_opinions-law-developments_report.pdf.

⁵⁸ Reported in *The Houston Chronicle*, June 2, 2006. See Roper, "Vinson & Elkins Settles with Enron for \$30 million," available at <http://www.chron.com/dispatch/story.mpl/special/enron/3921779.html>.

⁵⁹ 2008 WL 1995216 (S.D. Ohio 2008).

⁶⁰ 47 The Bus. L. (ABA) 167 (Nov. 1991).

⁶¹ 18 Mass. L. Rep. 598, 2004 Mass. Super. LEXIS 571 (Dec. 3, 2004).

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law firm did not require Dean Foods to disclose the matter and, further, the law firm did not disclose the investigation in its “no litigation” confirmation. Several months after the closing it was learned that Dean Foods was the target of a grand jury investigation stemming from the same or similar issues as the investigation in which Dean Foods was a witness. The court found the law firm failed to conduct the inquiry it was required to make by customary practice, and held the firm liable.⁶²

In *Prudential Insurance Company of America v. Dewey, Ballantine, Bushby, Palmer & Wood*,⁶³ the court noted that in issuing an opinion letter the attorneys stated they had relied on certificates of public officials, corporate documents and records with respect to the accuracy of material factual matters “which were not independently established”; the remedies opinion offered that the documents would be legal, valid, binding and enforceable “in accordance with [their] respective terms”; and the opinion included exceptions for bankruptcy, insolvency, reorganization, and similar laws. The court found that the attorneys owed a duty of care to the opinion recipient, the attorneys met that duty of care and, because no procedural or substantive misrepresentations were made, summary judgment was properly granted in the law firm’s favor. The fact that a typographical error in a document on which the attorneys were opining resulted in a loss to the opinion recipient of more than \$92 million did not make the law firm liable to the opinion recipient.

Conclusion

Issuing a third-party legal opinion is a high stakes endeavor and should be undertaken only after becoming sufficiently informed on the client’s business, the transaction at issue and on the fundamentals of issuing such opinions. There is plenty of literature available to assist with learning the fundamentals of opinion giving and customary practice. As reflected in some of the case summaries above, understanding customary practice and the rules surrounding opinion giving should not be overlooked, as they can lead to unwelcome involvement in a lawsuit and potential liability.

⁶² See Glazer and Field, “*No Litigation Opinions Can Be Risky Business*,” 14 Bus. L. Today (July/August 2005). Interestingly Donald Glazer and Arthur Field were the opposing experts in the *Dean Foods* case.

⁶³ 80 N.Y.2d 377, 605 N.E.2d 318 (NY Ct. App. 1992). The opinion was issued in connection with the refinancing of a \$92,885,000 loan collateralized by a first preferred fleet mortgage on five vessels owned by U.S. Lines. One of the recorded documents referred to the amount due as \$92,885 and when U.S. Lines filed for bankruptcy, the lender incurred substantial losses.

Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions, 63 The Business Lawyer (ABA) 1277 (August 2008)

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At the closing of many business transactions, the lawyers for one party deliver to the other party a legal opinion letter covering matters the recipient has asked those lawyers to address. These opinion letters, also commonly known as closing or third-party legal opinions, are prepared and understood in accordance with the customary practice of lawyers who regularly give them and review them for clients.

Customary practice permit an opinion giver and an opinion recipient (directly or through its counsel) to have common understandings about an opinion without spelling them out. The use of customary practice does this in two principal ways:

1. It identifies the work (factual and legal) opinion givers are expected to perform to give opinions. Customary practice reflects a realistic assessment of the nature and scope of the opinions being given and the difficulty and extent of the work required to support them.
2. It provides guidance on how certain words and phrases commonly used in opinions should be understood. Customary practice may expand or limit the plain meaning of those words and phrases.

By providing content to abbreviated opinion language, customary practice permits the omission from an opinion letter of descriptions of the procedures that the opinion giver has performed and of many definitions, assumptions, limitations, and exceptions. Thus, it reduces the number of words needed to communicate complex thoughts. As a matter of customary practice, the explicit inclusion in an opinion letter of some but not all of these matters does not exclude others customarily understood to apply. A departure from customary practice is not implied and should not be inferred unless the departure is clear in the opinion letter.

The role of customary practice in third-party legal opinion practice is well established. The American Law Institute’s *Restatement (Third) of the Law Governing Lawyers*¹ states:

In giving “closing” opinions, lawyers typically use custom and practice to provide abbreviated opinions that facilitate the closing. Such opinions

¹ The references to the *Restatement* in this statement are to Sections 51, 52, and 95 of the *Restatement*. The references also include the following Comments, Illustrations, and Notes to those sections: Section 51, Comment e; Section 52, Comment b, Comment e, Illustration 2; and Section 95, Reporter’s Note to Comment b, Reporter’s Note to Comment c. The *Restatement* sometimes refers to “custom and practice.” The *Restatement* uses the phrases “custom and practice” and “customary practice” to mean the same thing.

may not recite certain assumptions, limitations, and standards of diligence because they are understood between counsel.

The *Restatement* also refers to customary practice as an element in determining the “meaning of the opinion letter.”

The *Restatement* identifies customary practice as a source of the criteria for determining whether the opinion giver has satisfied its obligations of competence and diligence. Under the *Restatement* the “professional community whose practices and standards are relevant” in making that determination is that of “lawyers undertaking similar matters.” That professional community may vary based on, among other things, the subject of the opinion and the relevant jurisdiction.

The *Restatement* treats bar association reports on opinion practice as valuable sources of guidance on customary practice. Customary practice evolves to reflect changes in law and practice.

Some closing opinions refer to the application of customary practice. Others do not. Either way, customary practice applies.