

**FIRST AMENDED AND RESTATED REPORT OF
THE STATE BAR OF ARIZONA BUSINESS LAW
SECTION COMMITTEE ON RENDERING LEGAL
OPINIONS IN BUSINESS TRANSACTIONS,[†]
October 20, 2004**

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I. INTRODUCTORY MATTERS

A. *Purpose of This Report*

Parties to business and real estate transactions are often represented by legal counsel. In certain transactions a lawyer may be asked to deliver a written opinion to a party who is not the lawyer's client to further the recipient's due diligence inquiries and to confirm various legal aspects of a business or real estate transaction. Over the past two decades, various bar associations have reviewed and given guidance on "customary practices" governing these third party opinions in business transactions and have issued reports and policies that set forth the consensus of their membership as to the meaning and scope of third party opinions and the factual and legal investigation necessary to support the opinions.¹

In order to update its own third party opinion policy statement published in 1989,² in October of 2004 the Committee on Rendering Opinions in Business Transactions (the "Committee"), a committee of the Business Law

1. The Committee on Legal Opinions of the American Bar Association's Section of Business Law emphasized the role of customary practice in the giving of third party opinions by stating: "[T]he scope and the nature of the work counsel is expected to perform [is] based (whether or not so stated) on the customary practice of lawyers who regularly give, and lawyers who regularly advise opinion recipients regarding, opinions of the kind involved." American Bar Association Section of Business Law, Committee on Legal Opinions, *Legal Opinion Principles*, 53 BUS. LAW. 831, § I.B, at 832 (1998). The American Bar Association has also stated: "An opinion giver is entitled to assume, without so stating, that in relying on a closing opinion the opinion recipient (alone or with its counsel) is familiar with customary practice concerning the preparation and interpretation of closing opinions." American Bar Association Section of Business Law, Committee on Legal Opinions, *Guidelines for the Preparation of Closing Opinions*, 57 BUS. LAW. 875, §1.7, at 876 (2002) [hereinafter 2002 *Guidelines*]; see also RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 51(2) cmt. e, § 95 cmt. b (2000); The TriBar Opinion Committee, *Special Report of The TriBar Opinion Committee: U.C.C. Security Interest Opinions – Revised Article 9*, 58 BUS. LAW. 1453, 1455–56 (2003) [hereinafter 2003 *TriBar RA9 Report*]. See generally The TriBar Opinion Committee, *Third Party "Closing" Opinions*, 53 BUS. LAW. 591, § 1.4, at 600–03 (1998) [hereinafter 1998 *TriBar Report*].

2. This Report is intended to replace the *Report of the State Bar of Arizona Corporate, Banking, and Business Law Section Subcommittee on Rendering Legal Opinions in Business Transactions*, in 21 ARIZ. ST. L.J. 563 (1989) [hereinafter 1989 *Report*]. Since its publication, the 1989 *Report* has been widely used and generally accepted as a useful guide by practitioners in Arizona. Members of the Committee believed that no major departure was needed from the 1989 *Report*, but that this Report was appropriate for several reasons, including: (a) the evolution of new forms of entities not addressed by the original statement (notably, the limited liability company and limited liability partnership); (b) the increasing use of bankruptcy-remote entities and opinions relating thereto; and (c) intervening developments in law and in the practice of law.

Section of the State Bar of Arizona (the “Section”), prepared this policy statement (this “Report”) to update and summarize current customary practices with respect to rendering opinions of Arizona law in business and real estate transactions. Arizona business and real estate law practitioners should understand and adhere to these customary practices when requesting or rendering such opinions.

It should be noted at the outset that the consensus reached by various bar associations, including the American Bar Association, is that:

[a] third-party opinion is an expression of professional judgment on the legal issues explicitly addressed. By rendering a professional opinion, the opinion giver does not become an insurer or guarantor of the expression of professional judgment, the transaction or the future performance of the client. Nor does the rendering of an opinion guarantee the outcome of any legal dispute that may arise out of the transaction.³

Notwithstanding this consensus, however, practitioners are cautioned that their failure to prepare third party opinions within the norms of customary practices could expose them to liability to both the recipients of the opinion and to their own clients.

Although the need for and content of an opinion will vary depending on the type of transaction and the nature of the parties involved, the Committee hopes that suggesting model opinion language and related due diligence guidelines, as well as guidance regarding circumstances in which opinions might or might not be appropriate, will benefit our clients and enhance efficiency in business transactions by: promoting uniformity in opinion practice, leading to opinions that are better understood by business people, legal practitioners and the courts; reducing the often time-consuming and arduous process of negotiating third party opinions; matching the benefits of a thorough due diligence process to the costs of obtaining third party opinions to provide real value to the parties to the transaction; and reducing the number of requests for unnecessary or inappropriate opinions.

Article II of this Report generally discusses each section of the Illustrative Opinion appended to this Report and, where appropriate, suggests alternative opinion language and related due diligence procedures. In addition, to promote uniformity and understanding, this Report defines and discusses some words, phrases, and concepts which often arise in third party opinions. Article III discusses matters the Committee has concluded

3. Committee on Legal Opinions, *Third Party Legal Opinion Report, Including the Legal Opinion Accord, of the Section of Business Law, American Bar Association*, 47 BUS. LAW. 167, 171 (1991) [hereinafter *1991 Accord*].

are inappropriate subjects for third party opinions. Finally, Article IV of this Report addresses ethical and liability considerations involved in rendering third party opinions.

B. Use of This Report

This Report represents the consensus of the Committee members and was approved and adopted by both the Business Law Section and the Real Estate Section of the State Bar of Arizona in October of 2004. It is intended to serve as a guide to lawyers rendering opinions on Arizona law to third parties in business and real estate transactions. This Report does not articulate a minimum standard of care. This Report also is not intended to prescribe the exclusive means of conducting due diligence in connection with opinions; however, it does suggest that certain procedures and investigations should be sufficient, absent unusual circumstances that would prompt further inquiry (discussed in Section IV.B), to justify specified standard opinions.⁴

Much has been written about whether opinions should be standardized, about various means of standardization, and about the process of preparing opinions. The Committee has been cognizant of the multitude of other published materials on the subject and the diverse approaches espoused in those materials.⁵ In reviewing these matters, however, the Committee has recognized that some issues are unique to Arizona and that Arizona customs and practices may dictate different results.

The Illustrative Opinion is not intended to be used in its entirety for any one transaction. Although some of the opinions addressed in this Report are applicable to business or real estate transactions generally, many of the opinions are appropriate only under certain circumstances. In addition, this Report does not address each opinion that might be appropriate in a particular transaction.

Lawyers may incorporate this Report into their opinions. Some lawyers believe doing so will promote better understanding and interpretation of opinions. Other lawyers believe incorporating this Report might only

4. In the absence of a request for specific diligence, certain opinions should be understood to provide assurance that the opining lawyer has satisfied certain specified diligence procedures but that the opining lawyer may safely avoid additional, and possibly costly, diligence procedures in the absence of circumstances justifying further inquiry. *See infra* Sections II.A.4, II.B.1, II.D, IV.B.2.a. Likewise, where opining lawyers, with the consent of the recipient, use diligence procedures that rely for factual matters on certificates of others, certain opinions should be understood to imply no duty on the part of the opining lawyer to conduct additional diligence to establish the facts certified in the certificate. *See infra* Section II.A.5.

5. *See infra* Bibliography.

protract negotiations or create added expense. The Committee takes no position on this issue. If this Report is to be incorporated, the opinion should reference this Report as follows:

This opinion incorporates by reference, and is to be interpreted in accordance with, the First Amended and Restated Report of the State Bar of Arizona Business Law Section Committee on Rendering Opinions in Business Transactions, dated October 20, 2004.

C. Timing and the Role of Counsel

Because preparing and negotiating an opinion can be both costly and time-consuming, determination of whether or not any opinion is to be given should be resolved at the outset of the transaction (such as at the time a letter of intent, commitment letter, or other agreement in principle is concluded). Similarly, the negotiation of the scope of the opinion, the wording of the opinion (including assumptions and qualifications), and the identity of the lawyer who will render the opinion should begin at the earliest possible stage of the transaction.

A request for, or negotiation of, the opinion too often is left until the last minute. This places the lawyer rendering the opinion in a situation in which the lawyer might be unfairly portrayed as potentially “killing” the deal because of a refusal to render an opinion or because the lawyer may have insufficient time to perform the required due diligence. The lawyer asked to render the opinion may also be retained as “special” or “local” Arizona counsel and have limited knowledge of the parties and the transaction. Prior to requesting opinions, lawyers should consider whether it is more prudent, and in their own clients’ best interest, to conduct their own legal analysis of issues (including retention of local counsel) and whether an opinion from the adverse party’s counsel is really necessary or appropriate under the circumstances. In any event, a rule of reasonableness should be followed regarding requests for opinions so as to narrow the scope of opinions to those issues that are of legitimate concern to the recipients. Lawyers are strongly encouraged to follow the golden rule; i.e., do not request opinions from other lawyers which you would not give.⁶ This should help to avoid legal bills that are out of proportion to the nature of the transaction and to avoid overly adversarial, time-consuming, and costly negotiations between lawyers over nuances about which, truth be known, the respective clients seldom care.

6. See 2002 Guidelines, *supra* note 1, at 878.

II. FORM AND ELEMENTS OF OPINION

A. *Introduction*

1. Description of Role of Counsel

The first paragraph of the opinion lays the framework for the substantive information the recipient of the opinion will receive from the opining lawyer. The opining lawyer normally states in this paragraph the capacity in which the lawyer acted in the transaction. This provides the recipient with both a description of the party the lawyer represents and the scope and nature of the representation.

The statement indicating the opining lawyer's client prevents the recipient from believing that an attorney-client relationship exists between the opinion recipient and the opining lawyer. Often, opining lawyers will use the following phrases: "we are counsel to the Company," or "we have acted as local counsel to the Company in connection with the Transaction and do not otherwise represent the Company."

Opining lawyers often describe the capacity in which they acted in rendering an opinion to inform the recipient of the opining lawyer's familiarity with the client's affairs. A statement that the opining lawyer is "in-house" or "general counsel" may imply, among other things, that the opining lawyer is generally familiar with the client's affairs. A statement that the opining lawyer is "special counsel," or specially employed by the client in connection with the transaction, may imply that the lawyer is not generally familiar with the client's affairs. Based on inferences, an argument might be made that a "general counsel" has a higher duty to know or investigate than a lawyer designated as "counsel" or "special counsel." An argument also might be made that the designation "special counsel" somehow implies "special" knowledge or expertise.

The Committee does not believe that the lawyer is required to negate or address such inferences because the underlying facts (rather than the nomenclature used to describe the lawyer's role) ought to govern such issues. References such as "general counsel" or "special counsel" should not affect the scope of the opinions and should not increase or decrease the duty of the lawyer to conduct the investigation necessary to render the opinion.

Notwithstanding the Committee's view, in an abundance of caution, there is an increasing majority of opining lawyers that will use the phrase "counsel" to avoid any argument or implication that the opining lawyer should be held to a higher standard of knowledge. When an opining lawyer

is retained on the particular transaction as either local counsel or counsel for a particular area of law (e.g., tax or bankruptcy), however, many practitioners still describe their capacity in terms of the specialization to alert the recipient to the scope and nature of the opining lawyer's representation.

2. Jurisdictional Limitations

Lawyers usually limit their opinions to the law of certain jurisdictions. The Illustrative Opinion provides:

We are qualified to practice law in the State of Arizona, and we do not purport to be experts on, or to express any opinion concerning, any law other than the law of the State of Arizona and applicable federal law.

With the increase in multi-jurisdictional practice and firms, an alternative formulation could read:

We do not purport to express any opinion concerning any law other than the law of the State of Arizona. Although certain members of this firm are admitted to practice in other states, we have not examined the laws of any state other than the State of Arizona [and/_____/and federal law] nor have we consulted with members of the firm who are admitted in other jurisdictions with respect to the laws of such jurisdictions.

Provided that the opining lawyer has the relevant expertise, it is not unusual for a lawyer to include the general corporate statutory laws of Delaware or Nevada in the statement of laws addressed in the opinion in order to accommodate basic opinions relating to Delaware and Nevada entities, including due formation, good standing, power and authority, and due authorization.⁷ For example:

. . . and, with respect to the opinions expressed in the _____ numbered paragraph above, solely the statutory provisions of the [corporate], [partnership], or [limited liability company] laws of the State of Delaware.

Regardless of the jurisdictions mentioned, the general consensus among opinion committees and experts is that the term "law(s)," as used in the jurisdictional limitation, refers to the statutes, judicial and administrative

7. Although less frequent, and provided they have the relevant expertise, some Arizona lawyers opine as to California entities and include California corporate law in the laws addressed in the opinion.

decisions, and governmental rules and regulations in the applicable state or at the federal level. The term should not be read to include local or municipal statutes, codes, judicial and administrative decisions, or governmental rules or regulations *unless expressly included by the opining lawyer*.⁸

3. Statement of Reliance and Assumptions Based Upon Opinions of Other Counsel

Occasionally, due to lack of pertinent information, expertise in the subject matter, or expertise in local law, opining lawyers (“primary opining lawyers”) are unable to give certain opinions that are required to be rendered in connection with their opinion (“primary opinion letter”). When this circumstance arises, another opining lawyer (“secondary lawyer”) will be retained to provide an opinion (“secondary opinion letter”) addressing matters that the primary opining lawyer could not address. Reliance shall be placed on secondary opinion letters only with the written permission of the (a) recipient and (b) secondary lawyer, and it is best to affirmatively state such permission within the secondary opinion letter itself. An example of such permission is as follows:

The primary opining lawyer may rely on the opinions set forth in paragraphs ___, ___ and ___ of this letter in rendering its opinion furnished pursuant to Section ___ of the _____ Agreement.

In addition, the primary opining lawyer should (a) state any such reliance on a secondary opinion letter in the primary opinion letter and (b) deliver a copy of the secondary opinion letter upon which reliance is placed. For example, the Illustrative Opinion provides:

Insofar as our opinion pertains to matters of _____ law, we have relied upon the opinion of [firm name], of [city], [state] dated _____, a copy of which is attached.

By relying on a secondary opinion letter, a primary opining lawyer implies that it is reasonable to do so. If requested, it is reasonable for the primary opining lawyer to state that reliance is justified. Generally, to establish the reasonableness of reliance, the primary opining lawyer rendering the opinion should ascertain (a) whether the secondary opinion letter on its face responds to the questions posed, and (b) whether the primary opining lawyer should have any reason to question the competence

8. See 2002 *Guidelines*, *supra* note 1, app. § II.C, at 883; *Legal Opinion Principles*, *supra* note 1, § II, at 832–33; see also 1991 *Accord*, *supra* note 3, § 19, 215–17.

of the secondary lawyer. Establishing the reasonableness of reliance may require some inquiry if, for example, the secondary opinion letter on its face seems implausible or is not understandable. For instance, it is generally not reasonable for the primary opining lawyer to rely on a secondary opinion letter that was rendered by a secondary lawyer for a different transaction.⁹

Subject to the reasonableness of relying on the secondary opinion letter discussed above, the primary opining lawyer, simply by relying on a secondary opinion letter in rendering the primary opinion letter, does not assume responsibility to investigate or otherwise verify the opinions of the secondary lawyer. On the other hand, if the primary opinion letter states that it is in “concurrence” or “satisfaction” with the secondary opinion letter, the primary opining lawyer may be subject to broader responsibility, and such responsibility may require some independent investigation of law. Accordingly, the use of such terms is generally discouraged.¹⁰

Alternatively, a recipient separately may accept a secondary opinion letter regarding those matters that are not addressed in the primary opinion letter. This may be preferable in the case where a primary opining lawyer has no knowledge about the secondary lawyer or the amount of diligence undertaken by the secondary lawyer.¹¹ In that case, the primary opinion letter should either (a) expressly assume the correctness of the matters stated in the secondary opinion letter or, preferably, (b) entirely exclude such matters covered in the secondary opinion letter. By excluding such matters from the primary opinion letter (rather than assuming accuracy), the primary opining lawyer may avoid the issue of reasonable reliance altogether.

4. Recitation of Documents and Matters Examined

Lawyers use several methods to refer to the documents examined in preparation for rendering an opinion. Some lawyers do not specify the documents examined, but merely recite that the lawyer has examined “such documents and made such investigations deemed necessary in rendering the opinion.” Others list every document examined. A reasonable compromise approach may be to list those documents that are material to the transaction and also to state that the opining lawyer has examined:

such other documents as deemed necessary.

9. See 1998 *TriBar Report*, *supra* note 1, § 5.4, at 639.

10. See 2002 *Guidelines*, *supra* note 1, § 2.2, at 877.

11. See 1998 *TriBar Report*, *supra* note 1, § 5.5, at 639–40.

Absent limiting language in the opinion, it is customary for recipients to presume that the opining lawyer has reviewed such documents and undertaken such diligence in the opining lawyer's professional capacity, as is necessary to provide the requested opinions.¹²

When an opining lawyer has a relatively limited role, however, such as when acting as local counsel or performing the role of a secondary lawyer, it may be more appropriate to limit the extent to which the recipient presumes the scope of opining lawyer's due diligence by reciting all of the due diligence performed by the opining lawyer.¹³ This can be accomplished by the following limiting language:

We have examined only the following documents and have made no other investigation or inquiry.

Although limiting the examination to a particular list of documents and also to the opining lawyer's knowledge (without inquiry) as of the date of the opinion may have a significant effect on the scope of such opinions, the cost-benefit analysis of those limitations frequently is acceptable to the recipient. This is so especially when the opining lawyer has a limited role in the transaction or, because of particular circumstances, the opining lawyer has not formed or does not have a long-standing relationship with the client.

5. Officer's Certificates

This Report includes an illustrative officer's certificate in Appendix B ("Illustrative Officer's Certificate"). The Illustrative Officer's Certificate is intended to be a source of factual information and a guide for the opining lawyer in rendering opinions. It is important to note that any officer's certificate shall be prepared in light of the nature of the particular transaction, the parties involved, and the opinions to be given. The Illustrative Officer's Certificate is intended to be used as a starting point for consideration of issues arising from the Illustrative Opinion, and the additional officer's certifications set forth in this Section II.A.5 and elsewhere in this Report are intended for consideration of issues that arise from opinions that go beyond the Illustrative Opinion.

Use of the certifications in either the Illustrative Officer's Certificate or elsewhere in this Report should be tempered by three important limitations. First, no officer's certifications should be requested as to strictly legal

12. It is important to realize that there is a direct relationship between the quantity of documents examined and the value of the opinion qualified by the phrase "to our knowledge" or words of similar import. *See also id.*, § 1.4(d), at 602-03 (discussing misleading opinions).

13. *See id.*, § 1.5, at 603.

matters. Second, no officer's certifications should be requested if it is not necessary to support a requested opinion (many of the certifications suggested in this Report may be rendered unnecessary if the opining lawyer is entitled to rely on factual representations made by the company in the transaction documents, as the Illustrative Opinion provides). Third, to the extent that officers' certifications go beyond the representations made by the Company¹⁴ in the transaction documents, the opining lawyer should consider whether the certifications are creating liability for the client that are appropriate given the negotiated representations in the transaction documents and whether the opining lawyer should explicitly disclose such potential liability at the time the officer certifications are requested.

An officer's certificate can be used as a tool for the opining lawyer to obtain factual information about the client company, but the opining lawyer must determine whether additional independent due diligence is necessary to give the opinions contained in the opinion. Depending on the substance of an officer's certificate, the nature of the transaction, and the opinions contained in the opinion, it may also be appropriate for the opining lawyer to conduct additional independent due diligence relating to particular matters disclosed in the officer's certificate to buttress the conclusion that the officer's certifications are reasonably complete and accurate and that the opining lawyer has sufficient factual information to render the opinions contained in the opinion. It is important that an officer's certificate contain a meaningful narrative as to the facts and circumstances upon which the opinions are based. An officer's certificate should neither simply recite the opining lawyer's opinions nor reach legal conclusions that are to be reached by the opining lawyer.

In order to provide complete and accurate certifications about such factual matters, the officer of the client company providing the officer's certificate must be sufficiently familiar with: (i) the transaction in question; (ii) the general nature and scope of the Company's business operations; and (iii) the organizational structure of the Company. If an individual officer does not have sufficient general knowledge of the Company's business operations, structure, or the transaction, it may be prudent for the opining lawyer to obtain certificates from more than one officer or perform additional independent due diligence sufficient to support the assertions given in the opinion. Paragraphs one through four of the Illustrative Officer's Certificate contain sample language relating to the officer's

14. References to the "Company" in this context refers to any type of business organization, including corporations, limited liability companies, and various forms of partnership. Accordingly, the related references herein to an officer or officer's certificate should include certificates of members, managers, and general or other partners, as applicable.

familiarity with the transaction, the Company's business, and general organizational structure.

As noted above, an officer's certificate must always be specifically tailored to the opinions to be delivered by the opining lawyer. The opinion should be limited to subjects on which the opining lawyer should be able to form an opinion based on the documents the lawyer has been furnished and the legal principles involved. Occasionally, an opining lawyer will be required to include in the opinion matters upon which are outside the scope of legal representation and knowledge of the opining lawyer. The officer's certificate should be limited to those matters upon which the opining lawyer must rely on to issue the required opinion. For example, if an opinion addresses the status of the Company, an appropriate officer's certificate should include certifications encompassing the officer's knowledge relating to entity formation, existence, status, and authorization of the Company. Examples of some of the kinds of statements that may be included follow. All such statements should be limited to the actual knowledge of the signer by a general statement to that effect (an example appears in the first paragraph of Appendix B). An officer's certificate could include additional language (to the extent such statements are accurate) describing the documents reviewed by the officer as follows:

Attached hereto is a true and correct copy of the [ORGANIZATIONAL DOCUMENTS] of the Company and all amendments in effect as of the date hereof (the "Organizational Documents"). The [ARTICLES OF INCORPORATION] [ARTICLES OF ORGANIZATION] [CERTIFICATE OF LIMITED PARTNERSHIP] were/was accepted for filing on [DATE] and, to my knowledge, have/has never been withdrawn or revoked. No action has been taken by the Company or its [DIRECTORS] [MEMBER(S)] [MANAGER(S)] [PARTNERS] in contemplation of the filing of any further amendment or other document affecting the Organizational Documents.

The Company's Organizational Documents (including all amendments thereto or restatements thereof, if any) do not prohibit or restrict any of the activities that currently comprise the business operations of the Company. There are no agreements, covenants, or other instruments, internal or otherwise, which [materially] prohibit or restrict the business operations of the Company or the Transaction.

The Company has filed all annual reports, financial statements, and other documents or instruments required to be filed with any and all agencies or instrumentalities of [STATE OF

ORGANIZATION AND STATE OF FOREIGN QUALIFICATION OR REGISTRATION (IF ANY)] and has paid all filing fees, franchise taxes, and other sums, however designated, required to be paid in connection with any such filing, or otherwise, to maintain its existence, qualification to do business, and good standing in [STATE OF ORGANIZATION AND STATE OF QUALIFICATION OR REGISTRATION (IF ANY)].

As of the date hereof, no judicial proceeding is pending or, to my knowledge, has been threatened by any governmental authority alleging the existence of facts or circumstances that would make proper the dissolution or termination of the Company or, if proven to be true, would [materially] affect the Company's business or prospects. No notice of winding up or articles of termination has been filed with the [STATE OF ORGANIZATION], no resolution or action of the [BOARD OF DIRECTORS] [SHAREHOLDERS] [MEMBER(S)] [MANAGER(S)] [PARTNERS] of the Company approving such filing has been adopted, and no petition has been filed in any court of competent jurisdiction to dissolve or terminate the Company.

All federal, state, and local tax returns have been filed and all payments which are due and owing have been paid to the proper authorities or appropriate extensions have been granted or obtained.

Attached hereto is a true and correct copy of the [TITLE OF CORPORATE RESOLUTIONS], dated as of _____, 20____, containing resolutions duly adopted by the Company; such resolutions have not been amended, modified, or rescinded and remain in full force and effect on the date hereof. I have delivered all documents and information pertaining to the Company's Organizational Documents, minutes, resolutions, and written actions relating to the execution, delivery, or performance of the documents and the consummation of the transaction.

By way of additional example, if an opinion regarding pending or threatened litigation or alternative dispute resolution proceedings is required (as more specifically discussed in Section II.B.4) the officer's certificate could include language (to the extent such statements are accurate) similar to the following:

Attached hereto is a list of all judgments, orders, rulings, regulations, writs, injunctions, or decrees of any government, governmental instrumentality, or court, domestic or foreign, by

which Company or its assets are bound and that could [materially]¹⁵ affect the Company's business (collectively, the "Judgments"). The Company is not in violation of any of the Judgments. I have no knowledge of any reason why the Judgments would be violated by, or conflict with, the execution and delivery of the Documents and the consummation of the Transaction. There is no [material] legal action, suit, litigation, arbitration, mediation, or other alternative dispute resolution proceeding, proceeding, inquiry, or investigation pending or to my knowledge threatened against the Company or its assets. The Company has not received any notices or other communications from any federal, state, or local governmental agents or other authority indicating that such agent or authority might bring any proceedings against or involving the Company, which, if adversely determined, would [materially] affect the Company's business or its ability to perform or comply with the Company's obligations and covenants under the Transaction Documents.

No proceedings by or against the Company have been commenced in bankruptcy or for reorganization and liquidation or the readjustment of debts of the Company under the Bankruptcy Code or any other law, whether state or federal, nor has the Company made an assignment for the benefit of creditors, admitted in writing its inability to pay debts generally as they become due, filed or had filed against it any action seeking an order appointing a trustee or receiver of all or a substantial part of the assets of the Company.

By way of additional example, if a "no conflicts" opinion as to the company's organizational documents, other agreements, disputes, judgments, orders, decrees, permits, licenses, or certificates is required (as further discussed in Section II.B.6), the officer's certificate should disclose all of the [material] agreements, judgments, disputes, orders, decrees, permits, licenses, or certificates affecting the transaction and the company's business operations. In this case, the officer's certificate could include language (to the extent such statements are accurate) similar to the following:

Attached hereto is a list of all [material] permits, licenses, and certificates issued to the Company or to which the Company is subject in connection with the Company's business operations (the

15. Qualifiers used in the officer's certificates such as "material" should mirror the language negotiated in the representations made by the client in the final documents.

“Permits”). The Company has complied with all proceedings, filings, and hearings necessary to obtain and maintain the Permits.

Attached hereto is a list of any and all bonds, debentures, notes, mortgages, deeds of trust, loan agreements, contracts, leases, joint venture agreements, sales agreements, noncompete agreements, territorial restrictions, franchise agreements, supply agreements, trademark agreements, tradename agreements, patents, or other agreements or instruments to which the Company is a party or by which the Company’s assets may be bound and that are [material] to the business operations of the Company (the “Material Agreements”).

There are no supplemental agreements, contemporaneous understandings, letters of understanding, or interpretation, or other documents or matters of any type relating to the Transaction that are not fully reflected in the Transaction Documents.

As of the date hereof, the Company is not in violation of or default under its Organizational Documents, or in the performance or observation of any [material] obligation, agreement, covenant, or condition contained in any of the Material Agreements.

The opining lawyer should always review the referenced documents and Material Agreements in conjunction with the opining lawyer’s other due diligence prior to issuance of the opinion. The opining lawyer may also assist the officer in determining which documents, agreements, and other company information are [material] based on the nature of the Company’s business operations, the type of transaction, and the opinions to be given.

As discussed above, while the examples contained in this Section and the language contained in the officer’s certificate provide useful samples, they are not a substitute for the opining lawyer’s independent due diligence and are not exhaustive of the possible certifications necessary to render all opinions. An officer’s certificate should be tailored to address specific factual matters that fall within the scope of the opinions to be given by the opining lawyer.

B. Standard Provisions

1. Status of Entity

One of the most frequently requested opinions concerns an entity's organization. This section examines several entities as to which the lawyer may be requested to opine as to the entity's organizational status.¹⁶

a. Domestic Corporation

An opinion concerning the status of an Arizona corporation¹⁷ generally addresses organization, existence, and standing. The Illustrative Opinion provides:

The Company is a corporation [duly formed] [duly organized], validly existing, and in good standing under the laws of the State of Arizona.

The phrases "duly formed," "duly organized," "validly existing," and "in good standing" each impart a different meaning and should be considered separately when rendering an opinion as to the organizational status of an Arizona corporation.

Lawyers sometimes receive requests for the additional opinion that a corporation is "duly incorporated." Such an opinion is not warranted because the "duly incorporated" concept relates to the doctrine of de facto corporations that is not recognized in Arizona.¹⁸ Therefore, the phrases "is a corporation" and "duly incorporated" are redundant where applied to such entities.

i) Duly Formed

The opinion that a corporation is duly formed means that the corporation's corporate existence has begun under Arizona law and has not ceased. It is not an opinion that the entity has complied with all conditions

16. The opining lawyer must normally conclude that the formation and qualification of the entity involved is valid if the opining lawyer gives an opinion that the transaction documents are enforceable. *See infra* Section II.B.7. Customary requests for opinion letters ask for both opinions, which are generally given separately. Even if the request is only for an enforceability opinion, the opining lawyer must analyze and conclude favorably on entity formation and qualification.

17. A corporation which was formerly a foreign corporation but which has been domesticated in Arizona is a domestic corporation for all purposes. *See* ARIZ. REV. STAT. ANN. § 10-220 (2004).

18. *See id.* § 10-203; T-K Dist., Inc. v. Solderere, 704 P.2d 280 (Ariz. Ct. App. 1985).

precedent or subsequent to incorporation or that such compliance has been confirmed or waived by the Arizona Corporation Commission (“ACC”).

The opinion should be supported by review of a copy of the articles of incorporation, all amendments thereto, and all articles of merger or consolidation, each bearing a stamp indicating that they have been filed with the ACC. Corporate existence begins when (or on the day that) the articles of incorporation and certificate of disclosure are delivered to the ACC for filing.¹⁹ If a delayed date is specified, the delayed date will be the effective date if it is after the delivery date.²⁰ Filing is not conclusive evidence as against the State of Arizona (the “State”) in a proceeding by the State to revoke or cancel the filing or for involuntary dissolution, and the opinion should not be read to mean that the State will not succeed in any such action.

If the corporation was formed under statutes in existence prior to the Arizona Business Corporation Act that became effective July 1, 1976 (the “1976 Act,” which was replaced effective January 1, 1996 by the present Arizona Business Corporation Act), the opining lawyer should confirm that the corporation’s term of existence has not expired.²¹ The opining lawyer should not opine that an entity formed prior to the 1976 Act is a de facto corporation because of existing case law relating to the abolition of the de facto corporation doctrine.²²

This Report does not address issues involved where technical defects, such as failure to timely publish the articles of incorporation, failure to timely file the affidavit of publication, or failure to file an original or an amended certificate of disclosure, occurred in the incorporation process. If the opining lawyer determines that any defects exist, the lawyer must determine whether the existence of the defects are inconsistent with the opinion being given; if so, the opinion should be revised or the opining lawyer should insist that the defects be cured.

ii) Duly Organized

The opinion that a corporation is duly organized means that the corporation is duly formed, but is also an opinion that the internal

19. ARIZ. REV. STAT. ANN. § 10-203(A).

20. *Id.*

21. The statutes in effect prior to July 1, 1976, also required a number of provisions to be in articles of incorporation which are no longer required (such as limited term of existence and limitations on corporate debt). Those provisions in articles of incorporation remain in effect until they are amended, even though they are no longer required.

22. *See, e.g.,* Booker Custom Packing Co. v. Sallomi, 716 P.2d 1061, 1063 (Ariz. Ct. App. 1986) (observing Arizona’s abolition of the doctrine of defacto incorporation).

organization of the corporation is consistent with law. If an opinion is given that a corporation is duly organized, an opinion that it is duly formed is redundant and should not be given.

The “duly organized” opinion means that sufficient steps following incorporation have been taken to complete the organization of the corporation as required by law. Because the statutory presumption of Arizona Revised Statutes (“A.R.S.”) Section 10-203(A) only applies to incorporation and not to completion of the organization of the corporation,²³ the opining lawyer should confirm that certain matters of organization have been completed.

In order to determine whether a corporation has been “duly organized,” the opining lawyer should review the corporate records to confirm the existence of minutes of an organizational meeting or of a unanimous consent of directors in lieu of the meeting and, the opining lawyer should review records of the ACC to determine that no technical defects exist. If minutes are used, the corporate minute book should contain either evidence of proper notice of the meeting or written waiver of such notice. If a consent in lieu of meeting is used, it must be signed by all directors.

The opining lawyer should further confirm that bylaws were adopted, that the corporation has elected or appointed officers that are prescribed by statute by the board of directors, either at the organizational meeting or by unanimous written consent of the directors, in accordance with the bylaws, and that the scope of the directors’ responsibilities and authority are set forth in the bylaws. The opining lawyer should also confirm that at least one share of stock has been issued and that the corporate records reflect that the corporation has received valid consideration for the stock.

This portion of the “duly organized” opinion does not mean that the corporation’s management and capitalization are sufficient to avoid piercing the corporate veil, but only means that the corporation’s organization is free from any defects that would leave the corporation without sufficient power and authority to enter into the transaction. Where a defect in organization exists, such as the vacancy of an office prescribed by statute,²⁴ the opining lawyer should consider whether the “duly organized” opinion should be qualified or whether the defect should be cured. If the defect is not cured, the opining lawyer should qualify the opinion and disclose the defect if the opining lawyer believes the defect may be material.

23. See ARIZ. REV. STAT. ANN. § 10-203(A).

24. See *id.* § 10-840.

iii) Validly Existing

The opinion that a corporation is validly existing means only that the entity exists in the corporate form as of the date of the opinion. It does not mean that no ground for involuntary dissolution exists or that proceedings for dissolution (voluntary or involuntary), merger, or consolidation have been commenced. Nevertheless, if the opining lawyer knows that dissolution, merger, or consolidation are imminent, such information should be disclosed to the recipient of the opinion.

The opining lawyer's review may include searching the ACC's records and obtaining an officer's certificate containing representations of fact sufficient to permit the inference that the entity continues to exist in the corporate form. In the case of pre-Arizona Business Corporation Act corporations (corporations formed before July 1, 1976), the opining lawyer should confirm that the corporation's term of existence has not expired. In addition, because this opinion covers the present status of the Company, the opining lawyer should obtain and review a current good standing certificate (as discussed in the next section of this Report) as evidence that the Company is a corporation.

iv) Good Standing

The opinion that a corporation is in "good standing" is generally understood to mean that the corporation's corporate status has not been revoked by the jurisdiction of its formation for failure to file any required annual or other reports, pay franchise taxes, and/or comply with other applicable requirements.²⁵ The opinion is usually given based solely upon obtaining a recently dated good standing certificate from the jurisdiction of the corporation's formation and/or foreign qualification.²⁶

The Arizona Business Corporation Act provides that anyone may apply to the ACC for a certificate of good standing for either a domestic or foreign corporation.²⁷ The certificate will set forth the corporation's name (or the name a foreign corporation is using in Arizona, if it is qualified under a name other than its true name), the date on which it was incorporated or authorized in Arizona, and a statement that all affidavits, filing fees, and reports required before the date of the certificate have been filed or paid.²⁸ The good standing opinion does not mean the corporation is in compliance in all respects with the Arizona Business Corporation Act or

25. *Id.* § 10-128(B).

26. *Id.* § 128(A).

27. *Id.*

28. *Id.*

with any other laws applicable to Arizona corporations, or that the corporation has paid applicable taxes or filed required forms or returns relating to taxes.

In the event of any substantial interval between the date of the certificate of good standing and the date of the opinion, the opining lawyer should either state that the opinion is rendered only as of the most recent date of confirmation or, as noted in the next Section of this Report, consider ascertaining whether any report or tax payment date has intervened between the most recent date of confirmation and the opinion date, and obtain an updated officer's certificate regarding report filing and tax status.

Prior to giving an opinion that a corporation is in good standing, the opining lawyer should obtain a certificate of good standing from the ACC (or at least verify telephonically from the ACC that the ACC will issue the certificate, in which case the opining lawyer should order the certificate to be issued by the ACC in due course) and should rely on that certificate in giving the opinion.

v) Tax Clearance

An Arizona income tax statute "suspends" the corporate powers, rights, and privileges of a domestic corporation if certain Arizona income taxes, penalties, jeopardy or fraud assessments, or interest are not paid within specified times.²⁹ The suspension becomes effective upon transmission from the Department of Revenue to the ACC of the name of the delinquent corporation.³⁰ In practice, the Department of Revenue has rarely, if ever, commenced proceedings under this statute. The law provides that contracts made by a suspended corporation are voidable at the instance of any party other than the taxpayer.³¹

To date, general Arizona practice has been to give a good standing opinion without consideration of, or due diligence with respect to, this statute. If the Department of Revenue invokes the statute, documents to that effect should be placed in the file of the corporation at the ACC and the ACC should not give a certificate of good standing.³²

A lawyer may expressly disclaim an opinion about this statute in connection with a good standing opinion either by assuming that the corporation has complied with its terms or by qualification of the opinion to exclude the statute. An appropriate assumption could state:

29. See ARIZ. REV. STAT. ANN. § 43-1152 (1998 & Supp. 2005).

30. *Id.* § 43-1153.

31. *Id.* § 43-1155.

32. The ACC does not have a specific policy or procedure about this matter.

We assume that the corporation has paid all income taxes, fines, jeopardy or fraud assessments, and interest due from it and payable to the State of Arizona.

A qualification of the opinion could state:

We express no opinion about the effect on the corporation or the Transaction, if any, of the provisions of Arizona Revised Statutes § 43-1152 *et seq.*

In light of the general practice discussed above, the failure to make an assumption or qualification should not imply that the opinion addresses this statute; however, a lawyer who knows that a corporation is in violation of this statute should not render an opinion that the corporation is in good standing.

In order to give an opinion about this statute a lawyer should secure either: (i) a certificate from an officer of the corporation as to its payment of taxes, fines, jeopardy or fraud assessments, and interest, or (ii) a tax clearance certificate from the Department of Revenue pursuant to the statute.³³

The tax clearance certificate is based on the Department of Revenue's records, including the returns filed and certified by the corporation.³⁴ Accordingly, a backup certificate from the corporation is not necessary unless the Department of Revenue's tax clearance certificate is qualified.

vi) General Comments

The opinions relating to due formation, due organization, valid existence, and good standing do not mean that the corporation has obtained any particular licenses, registrations, or approvals, except any required by the Arizona Business Corporation Act.

b. Domestic Partnership

i) General Partnership

An opinion concerning the status of an Arizona general partnership generally addresses formation and continued existence. The Illustrative Opinion provides:

The Company is a validly existing Arizona partnership.

33. See ARIZ. REV. STAT. ANN. § 43-1151 (1998).

34. *Id.*

The above opinion means that a general partnership has been formed under Arizona law and continues to exist on the date of the opinion. There is no distinction between “duly formed” and “duly organized” with respect to partnerships, because the law does not impose additional requirements after formation.

Both the specific provisions of the Arizona Partnership Act³⁵ and the common law of the State of Arizona, which the Arizona Partnership Act codifies, apply to determine the existence of an Arizona general partnership. There is no particular formality to the formation of an Arizona general partnership and no particular content is required for an Arizona general partnership agreement. Rather, the Arizona standard is one that takes into account all facts and circumstances, principally the intent of the parties. A partnership may file a Statement of Partnership Authority with the Arizona Secretary of State by which it places on the public record the fact that the partnership exists and designates those persons or entities who are partners and who are authorized to act on behalf of the partnership.³⁶

Generally, this opinion is given in instances where there exists a written partnership agreement. The Committee makes no recommendation regarding opinions respecting de facto partnerships, partnerships by estoppel, or other non-written partnership agreements. Further, if a partnership purports to have been formed under the laws of another state, it may be appropriate to consult a lawyer in the state of formation prior to rendering an opinion about its existence.

The opinion should be substantiated by a review of the applicable partnership agreement to determine that two or more persons or entities associated with one another as co-owners of a business for profit at the time the partnership was formed.³⁷ The opining lawyer should also ascertain that none of the causes of dissolution (including expiration of the stated term of the partnership) set forth in A.R.S. section 29-1071 has occurred or is in process.³⁸ Any “Statement of Partnership Authority” should also be reviewed and, if none has been filed, consideration should be given to requiring such filing prior to issuance of the opinion. Filing is not required by law, and the opinion can be given even if no such statement has been filed, but the existence of such a filing is additional evidence of due formation of the partnership.

35. See generally Uniform Partnership Act, ARIZ. REV. STAT. ANN. §§ 29-1001 to -1111 (1998 & Supp. 2005).

36. *Id.* § 29-1023 (1998).

37. *Id.* § 29-1012(A).

38. See *id.* § 29-1071.

The opining lawyer should also determine the domicile of any entities that have general partners. If the general partners are all foreign entities, or if the general partner that is to act for the partnership in Arizona is a foreign entity, qualification of one or more of them in Arizona may be required by the applicable law governing such entities.³⁹ The qualification or non-qualification in Arizona of the partners should not affect the opinion about the existence of the partnership, but the opining lawyer should consider whether non-qualification of a partner affects any of the other opinions rendered.

Although a certificate of fictitious name may need to be recorded for other purposes, recording of a certificate is not necessary for the formation or existence of a general partnership.⁴⁰

ii) Limited Partnership

An opinion about the status of an Arizona limited partnership generally addresses formation and continued existence. The Illustrative Opinion provides:

The Company is a limited partnership, duly organized and validly existing under the Arizona Uniform Limited Partnership Act.

The phrases “duly organized” and “validly existing” are customarily used in rendering a limited partnership status opinion. Unlike the use of these phrases in a corporate status opinion, where each phrase has a separate meaning, the Committee recommends that they be considered as a single unit when used in a limited partnership status opinion. The opinion means that: (a) a limited partnership has been formed pursuant to the Arizona Limited Partnership Act, as in effect on the date of formation, for a purpose permitted under A.R.S. Section 29-306,⁴¹ and (b) the partnership continues to exist on the date of the opinion. There is no distinction between “duly formed” and “duly organized” with respect to partnerships, since the law does not impose additional requirements after formation.

For partnerships formed after July 24, 1982, this opinion means that a certificate of limited partnership has been filed in the office of the Arizona Secretary of State,⁴² that the certificate is in substantial compliance with the

39. See *id.* §§ 10-1501 to -1532 (2004 & Supp. 2005) (foreign corporations); *id.* §§ 10-11501 to -11531 (foreign nonprofit corporations); *id.* §§ 29-348 to -355 (1998 & Supp. 2005) (foreign limited partnerships); *id.* §§ 29-801 to -812 (foreign limited liability companies).

40. See *id.* §§ 29-102 to -103 (1998).

41. *Id.* § 29-306.

42. See *id.* § 29-308(A).

requirements of the statute,⁴³ that any amendments to the certificate of limited partnership substantially comply with the requirements of the statute,⁴⁴ and that the limited partnership has not been dissolved.⁴⁵ It is not an opinion that the certificate of limited partnership actually or completely complies with the statute. In the case of partnerships formed prior to July 24, 1982, other standards apply.⁴⁶

This opinion should be substantiated by a review of a copy of the certificate of limited partnership and all amendments, showing filing by the Arizona Secretary of State, and the limited partnership agreement, if any, in order to determine whether those documents substantially comply with the requirements of the Arizona Limited Partnership Act.

In addition, the opining lawyer should ascertain that no dissolution has occurred that is not reflected in documents of record at the Secretary of State's office.⁴⁷

iii) Limited Liability Partnership and Limited Liability Limited Partnership

An opinion concerning the status of an Arizona limited liability partnership ("LLP") or limited liability limited partnership ("LLLP") generally addresses formation and continued existence. The Illustrative Opinion provides:

The Company is a validly existing [general] [limited] partnership which has qualified as a limited liability partnership.

The above opinion means both that a general or limited partnership has been formed under Arizona law and that it has qualified as a limited liability partnership under Arizona law and continues to exist on the date of the opinion.

43. *See id.* § 29-308(B).

44. *Id.* § 29-309.

45. *See id.* §§ 29-344 to -345.

46. A limited partnership formed pursuant to a prior statute and existing on July 24, 1982, was required to file a certificate of amendment on or before December 31, 1984, containing the information specified in A.R.S. § 29-308(A), appointing an agent for service of process, and stating the place where the original certificate of limited partnership was filed or recorded. The failure to file such an amendment did not result in dissolution or affect the continued existence of the partnership. *Id.* § 29-308(A). However, the partnership cannot maintain an action in an Arizona court after December 31, 1984, until the certificate of amendment is filed. A.R.S. § 29-364 contains additional rules concerning existing limited partnerships' names, contributions and distributions, amendments, assignments, and other items. *See generally id.* § 29-364.

47. Although the filing of a certificate of cancellation is required upon dissolution, the filing of the certificate is not a prerequisite to the actual occurrence of the dissolution. *Id.* §§ 29-310, -344.

Either general or limited partnerships may become limited liability partnerships in Arizona, and the same procedure applies to both.⁴⁸ The partnership must file a statement of qualification pursuant to A.R.S. Section 29-1101 and the additional publication and annual reports requirements of A.R.S. Section 29-1103 must be observed.⁴⁹ Before rendering the opinion, the opining lawyer should verify that the general or limited partnership has been validly formed and that appropriate entity authority exists for filing the Statement of Qualification (by provision for authority to so file in the organizational documents, or by the consent of the partners).⁵⁰ In addition, the opining lawyer should review a copy of the Statement of Qualification filed with the Secretary of State and verify that publication has occurred and all required annual reports have been filed.

iv) General Comments – All Partnerships

Because there is no statutory or regulatory authority for obtaining a “good standing” certificate for a partnership and because none are provided by the State, no opinion should be given that a partnership, general or limited, is in good standing in Arizona. The Secretary of State will issue a “Certificate of Existence” for limited or general partnerships that have filed certificates of limited partnership or statements of partnership authority. It is recommended that the opining lawyer obtain such a certificate in connection with rendering the opinion.

c. Limited Liability Company

An opinion about the status of an Arizona limited liability company (“LLC”) generally addresses formation and continued existence. The Illustrative Opinion provides:

The Company is a limited liability company validly existing under the laws of the State of Arizona.

The opinion means that (a) articles of organization have been filed with the ACC and (b) neither articles of termination nor certificate of dissolution have been filed with the ACC. The statute provides that the filing of articles of organization is conclusive evidence of compliance with all conditions

48. See generally *id.* §§ 29-1101 to -1109 (1998 & Supp. 2005). One difference is that only a limited partnership may use the designation “L.L.L.P.” or “Limited Liability Limited Partnership,” whereas either a general or limited partnership may use “L.L.P.” or “Limited Liability Partnership.” See *id.* § 29-1102.

49. *Id.* §§ 29-1101, -1103.

50. *Id.* § 29-367 (limited partnerships); *id.* § 29-1101 (general partnerships).

precedent required to be performed by the organizer(s) and the LLC has been legally organized and formed.⁵¹

Cause for dissolution of the LLC may exist which is not reflected by the filed articles of termination or certificate of dissolution. The ACC has authority to dissolve an LLC if, among other things, the LLC: (i) fails to make a required amendment to its articles of organization; (ii) fails to make a required publication or to file an affidavit of publication; or (iii) fails to maintain a statutory agent.⁵² In order to administratively dissolve the LLC, however, the ACC must file a certificate to that effect.⁵³ Even if the opining lawyer knows cause for dissolution exists, the LLC is validly existing until the certificate is filed.⁵⁴ The opining lawyer should, however, qualify the opinion to reflect actual knowledge of the existence of causes for administrative dissolution.

An LLC can also be dissolved by court order.⁵⁵ Although the statute is not clear, it appears that the existence of the LLC does not cease until articles of termination are filed.⁵⁶ The opinion that an LLC is validly existing does not mean that there has been no court order with respect to dissolution or winding up of the LLC unless articles of termination have been filed with the ACC. The opining lawyer should, however, qualify the opinion to reflect actual knowledge of the existence of any court order of winding up or dissolution.

The opining lawyer should order from the ACC and review a Certificate of Good Standing⁵⁷ with respect to the LLC prior to rendering an opinion as to valid existence. The opining lawyer should rely on that certificate in giving the opinion (and expressly so state in the opinion).

d. Foreign Corporation

An opinion about the status of a corporation formed under the laws of a foreign jurisdiction and doing business in Arizona is frequently requested. The Illustrative Opinion provides:

The Company [is a corporation, duly organized, validly existing, and in good standing under the laws of the State of

51. *Id.* § 29-635(B).

52. *Id.* § 29-786(A).

53. *See id.* § 29-786(C).

54. *Id.* § 29-784.

55. *See id.* § 29-785.

56. *See id.* § 29-784(A).

57. The “Certificate of Good Standing” may also be referred to as the “Certificate of Existence.”

_____ and] is qualified to do business as a foreign corporation under the laws of the State of Arizona.

Opinions of Arizona lawyers are customarily limited to the laws of the State of Arizona, and an opining lawyer usually does not give an opinion about the organization, existence, and good standing of a corporation formed under the laws of a jurisdiction in which the opining lawyer is not licensed to practice. In most cases that opinion is provided by local counsel in the jurisdiction of incorporation. Nevertheless, the Committee recognizes a general exception to this rule in the case of corporations or other legal entities formed under the laws of Delaware or Nevada as a result of the common choice of those jurisdictions as a state of formation. A lawyer rendering an opinion about the status of an entity formed under the laws of another jurisdiction, including Delaware and Nevada, should have sufficient knowledge of the laws of that jurisdiction and conduct the due diligence necessary to render the opinion (for example, terms such as “good standing” may have more comprehensive meanings in some jurisdictions).

An opinion that a foreign corporation is “qualified to do business as a foreign corporation under the laws of the State of Arizona” means that the corporation has filed an application for authority to transact business as a foreign corporation,⁵⁸ has published the application,⁵⁹ and its authority has not been revoked by the ACC.⁶⁰ This opinion should be substantiated by review of a copy of the filed application and a good standing certificate from the ACC. The tax clearance statute discussed in connection with domestic corporations is also applicable to foreign corporations and may affect the qualification opinion.⁶¹

This opinion does not mean that the opining lawyer has reviewed corporate records to determine whether defects have occurred in the incorporation or qualification process. Similarly, the opinion should not be read to suggest that the foreign corporation complies with all provisions of the Arizona Business Corporation Act, or other laws applicable to Arizona corporations, or that it has paid any applicable taxes in Arizona.

A lawyer may be asked to give an opinion about the qualification of an Arizona corporation to transact business in one or more foreign jurisdictions. A typical form of this requested opinion is:

58. See ARIZ. REV. STAT. ANN. § 10-1503(A) (2004).

59. See *id.* § 10-1503(D). The Committee does not take a position on due qualification in the circumstance where the publication was not timely. The opining lawyer in that circumstance must determine whether the defect is inconsistent with the opinion being given; if so, the opinion should be revised or the opining lawyer should insist that the defects be cured.

60. See *id.* § 10-1530.

61. See discussion *supra* Section II.B.1.a.v.

The Company is duly qualified to do business as a foreign corporation and is in good standing (a) in the State of _____, or (b) in each jurisdiction in which it owns or leases property or where the nature of its business requires it to qualify.

Opinions in the form of (a) above may be rendered in reliance on an opinion from appropriate local counsel or if the opining lawyer has sufficient knowledge of the law of the other jurisdiction. Opinions in the form of (b) above are not usually appropriate, because, in addition to requiring knowledge of the law of another jurisdiction, they require detailed knowledge of a company's business activities and property. Thus, the due diligence necessary to render this opinion may be time-consuming and expensive.

Occasionally, a lawyer may be asked to give an opinion that a non-client entity's activities in Arizona, including the making of a loan or acquisition, do not require it to qualify to do business as a foreign corporation in Arizona. The concept of "doing business" may depend on a court's interpretation of the level of a corporation's business or contacts in the state and therefore may not be determined with legal certainty. To give such an opinion, the opining lawyer must do sufficient due diligence about the non-client entity's business and contacts in Arizona before giving such an opinion—which may not be practicable or cost effective. Thus, if such an opinion is requested, the parties to the transaction should review whether or not such an opinion is appropriate and whether or not the opining lawyer is in a position to efficiently provide such an opinion, given the circumstances of that transaction.⁶²

e. Foreign Limited Partnership, Limited Liability Limited Partnership or Limited Liability Partnership

An opinion may be requested about the status of a limited partnership, limited liability limited partnership, or limited liability partnership formed under the laws of a foreign jurisdiction and transacting business in Arizona. The Illustrative Opinion provides:

Based solely on the [certificate of limited partnership filing dated _____, 20__, issued by the Arizona Secretary of State] [statement of foreign qualification filed with the Arizona Secretary of State of _____, 20 __], the Partnership is qualified to

62. In any event, a "doing business" opinion does not state or imply that the foreign corporation has complied with all applicable state laws, but only with A.R.S. Sections 10-1501. See ARIZ. REV. STAT. ANN. §§ 10-1501(B) (2004).

do business as a foreign limited [liability] [liability limited] partnership under the laws of the State of Arizona.

An opinion that a partnership is “qualified to do business as a foreign limited [liability] [liability limited] partnership under the laws of the State of Arizona” means that the partnership has submitted to the Arizona Secretary of State a proper application for registration as a foreign limited partnership,⁶³ or a proper statement of foreign qualification,⁶⁴ that the Secretary of State has filed the application and issued a certificate of registration (for limited partnerships and limited liability limited partnerships),⁶⁵ or has filed the statement of foreign qualification (for limited liability partnerships),⁶⁶ and that the registration (or statement) has not been cancelled.⁶⁷ This opinion should be substantiated by review of the application and the registration certificate. The Secretary of State will issue a certificate that an application has been filed and a certificate of registration has been issued, together with copies thereof, for foreign limited partnerships and limited liability limited partnerships, but will only issue a certified copy of the statement of foreign qualification for foreign limited liability partnerships.

This opinion does not mean that the opining lawyer has determined whether any defects have occurred in connection with the qualification of the foreign partnership other than those appearing on the face of the application or the certificate. This opinion also does not mean that the opining lawyer has reviewed partnership records to determine whether defects have occurred in the organization process or that the partnership validly exists under the laws of the foreign jurisdiction. Finally, the opinion should not be read to suggest that the foreign limited partnership complies with all provisions of the Arizona Limited Partnership Act⁶⁸ or other laws applicable to Arizona partnerships, or that it has paid any applicable taxes in Arizona. The opining lawyer should also consider whether the general partners of the foreign limited partnership must also qualify to transact business in Arizona.⁶⁹

63. *See id.* § 29-349 (1998).

64. *See id.* § 29-1106.

65. *See id.* § 29-350.

66. *See id.* § 29-1106.

67. *See id.* § 29-353.

68. *See generally* Revised Uniform Partnership Act, ARIZ. REV. STAT. ANN. §§ 29-301 to -376 (1998 & Supp. 2005).

69. The ACC and Secretary of State have not taken a position on this issue.

f. Foreign Limited Liability Company

An opinion may be requested about the status of a limited liability company formed under the laws of a foreign jurisdiction and transacting business in Arizona. The Illustrative Opinion provides:

Based solely on the Certificate of Registration issued by the Arizona Corporation Commission on _____, 20 __, the Company is qualified to do business as a foreign limited liability company under the laws of the State of Arizona.

An opinion that a limited liability company is “qualified to do business as a foreign limited liability company under the laws of the State of Arizona” means that the limited liability company has submitted to the ACC a proper application for registration as a foreign limited liability company,⁷⁰ that the ACC has filed the application and issued a certificate of registration,⁷¹ and that the registration has not been cancelled.⁷² This opinion should be substantiated by review of the application and the registration certificate. The ACC will issue a certificate that an application has been filed and a certificate of registration has been issued, together with copies thereof.

This opinion does not mean that the opining lawyer has determined whether any defects have occurred in connection with the qualification of the foreign limited liability company other than those appearing on the face of the application or the certificate. This opinion also does not mean that the opining lawyer has reviewed company records to determine whether defects have occurred in the organization process or that the company validly exists under the laws of the foreign jurisdiction. Finally, the opinion should not be read to suggest that the foreign limited liability company complies with all provisions of the Arizona Limited Liability Company Act⁷³ (“ALLCA”) or other laws applicable to Arizona limited liability companies, or that it has paid any applicable taxes in Arizona. The opining lawyer should also consider whether the managers (if any) of the foreign limited liability company must also qualify in Arizona. The ACC has taken the position on the staff level that such qualification is required and will not file applications for registration of foreign limited liability companies in which the managers are foreign entities not qualified in Arizona.

70. See ARIZ. REV. STAT. ANN. §29-802 (1998 & Supp. 2005).

71. See *id.* §29-803.

72. See *id.* §29-808.

73. See generally *id.* §§ 29-601 to -857.

2. Capitalization

a. Corporations⁷⁴

An opinion about a corporation's capitalization generally addresses due authorization, validity of issuance, and assessability of shares. The Illustrative Opinion provides:

The Company's authorized capital consists of _____ common shares, of which _____ shares are issued and outstanding. The Shares issued [pledged] in the Transaction have been duly authorized and are validly issued, fully paid, and nonassessable.⁷⁵

b. Due Authorization

Shares are duly authorized if the corporation: (1) has created the shares in accordance with applicable law and (2) has created the shares in accordance with its articles of incorporation, having a sufficient number of shares of each class or series authorized in the articles of incorporation to cover the issuance.⁷⁶

Confirmation that the shares were created in accordance with applicable law and the corporation's articles of incorporation requires verification that: (1) the substance of the provisions pertaining to the shares are sufficient to comply with the law and the articles of incorporation; (2) the shares do not possess any attributes that are prohibited by law or the articles of

74. This section of the report deals with corporations organized under the Arizona Business Corporation Act ("ABCA") and not other entities governed by Title 10, such as close corporations, professional corporations, nonprofit corporations, business development corporations, cooperatives, and sole shareholder corporations. *See* ARIZ. REV. STAT. ANN. §§ 10-120 to -1702 (2004). If the opinion that has been requested pertains to a corporation organized under any laws other than the ABCA, the opining lawyer must refer to the statutes applicable to the corporation in question.

75. Although the language of the Illustrative Opinion appended to the 1989 *Report, supra* note 2, app. A, at 610-16, contained the concept of "par value," the ABCA was revised after the publication of the 1989 *Report* and did away with this concept. Par value, in conjunction with the concept of "stated capital," was originally intended to protect creditors by revealing the amount of capital received by the corporation in exchange for the issuance of its shares. This was the minimum amount of permanent capital invested in the corporation and would not be available for distribution to shareholders until creditors of the corporation were satisfied. *See generally* MODEL BUS. CORP. ACT § 6.21 cmt. (1999) (provides historical background to concept of par value).

76. *See generally* ARIZ. REV. STAT. ANN. § 10-601 (2004); Scott FitzGibbon & Donald W. Glazer, *Legal Opinions in Corporate Transactions: The Opinion That Stock is Duly Authorized, Validly Issued, Fully Paid and Nonassessable*, 43 WASH. & LEE L. REV. 863, 866-74 (1986) (discussing what it means to opine that stock has been "duly authorized").

incorporation; and (3) the shares do not violate any restrictions imposed by law or set forth regarding the shares in the articles of incorporation.⁷⁷ Section 10-601 of the A.R.S. provides that the articles of incorporation must “prescribe the classes of shares and the number of shares of each class that the corporation is authorized to issue.”⁷⁸ If more than one class of shares is authorized, the articles of incorporation must prescribe a distinguishing designation for each class, and set forth the preferences, limitations and relative rights of each class before shares of that class may be issued.⁷⁹ The opining lawyer, therefore, must verify that the articles of incorporation actually set forth and establish the terms for the particular shares for which an opinion is requested. Furthermore, the articles of incorporation must authorize “[o]ne or more classes of shares that together have unlimited voting rights” and one or more classes of shares that together are entitled to receive the net assets of the corporation on dissolution (these shares may be the same as the shares that have the voting rights).⁸⁰

The corporation must also have taken the necessary steps to create the shares, i.e., the corporation took the necessary action, based on the laws then in effect, to adopt the provisions contained in the articles of incorporation relating to the shares and that those provisions continue in effect.⁸¹ Generally, minor defects in the procedures by which the articles of incorporation were adopted should not prevent an opining lawyer from giving the “duly authorized” opinion so long as the defect would not lead a court to refuse to recognize the existence of the shares or any of the material rights the shares purport to hold under the articles of incorporation.⁸²

Often, if a corporation has been in existence for a long time its corporate records with respect to proper authority may be incomplete or missing. If the opining lawyer determines that this is the case after reasonable

77. See FitzGibbon & Glazer, *supra* note 76, at 867. Generally, there are few restrictions imposed by law on the attributes that shares may possess, however, under the ABCA:

[a]t each election for directors, shareholders are entitled to cumulate their votes by multiplying the number of votes they are entitled to cast by the number of directors for whom they are entitled to vote and casting the product for a single candidate or distributing the product among two or more candidates.

ARIZ. REV. STAT. ANN. § 10-728(B) (2004). The ABCA also requires that all shares of the same class have preferences, limitations, and relative rights identical to those other shares of that class or to the extent otherwise provided in the description of the series, with those of other series of the same class. See *id.* § 10-601(A) to -602.

78. *Id.* § 10-601(A).

79. *Id.*

80. *Id.* § 10-601(B).

81. See FitzGibbon & Glazer, *supra* note 76, at 869.

82. *Id.* at 870.

investigation, the opining lawyer should be permitted to rely on the presumption of regularity and continuity (unless there is reason to doubt such an assumption) that the shares of the corporation were duly authorized.⁸³ If reliance on such a presumption is necessary, the opining lawyer should make a specific disclosure to that effect. For example, the opining lawyer may state:

In connection with our opinion in paragraph ____ above concerning the due authorization of the shares, our investigation revealed that certain corporate records concerning [specify the missing records and describe their relevance] were either missing or incomplete. As a result, we have relied on the presumption of regularity and continuity to the extent necessary to enable us to provide that opinion.⁸⁴

This presumption is not a legal doctrine but rather arises from practical necessity to avoid an unjustified expense of reviewing each authorization of, and resolution approving, the shares.⁸⁵ To determine the appropriateness of relying on this assumption, the opining lawyer must weigh the relative importance of the missing corporate records to the opinion being given.⁸⁶

The “duly authorized” opinion also requires confirmation that there were a sufficient number of authorized shares of the relevant class available at the time of the issuance.⁸⁷ The authorized number of shares may be verified by a review of the articles of incorporation, including all amendments. If there has been any redemption of shares by the corporation, the opining lawyer must confirm that there has been no amendment to the articles of incorporation that would prohibit the reissuance of those shares. If there has been such an amendment, the number of authorized shares is reduced by the number of shares acquired by the corporation, effective as of the date of the amendment of the articles of incorporation.⁸⁸ The number of issued shares

83. See 1991 *Accord*, *supra* note 3, § II.B, at 230; Florida Bar Opinion Committee, *Report on Standards for Opinions of Florida Counsel of the Special Committee on Opinion Standards of the Florida Bar Business Law Section*, 46 BUS. LAW. 1407, § IV.A., at 1439 (1991) [hereinafter 1991 *Florida Report*]; see also 2002 *Guidelines*, *supra* note 1, § 4.2, at 880 (acknowledging the advisability of weighing the expense and time required to engage in an extensive legal and factual inquiry versus the actual benefit of the opinion to the opinion recipient).

84. See 1991 *Accord*, *supra* note 3, § II.B, at 230.

85. 1991 *Florida Report*, *supra* note 83, § IV.A at 1439.

86. 1991 *Accord*, *supra* note 3, pt. II.B at 230; see also 2002 *Guidelines*, *supra* note 1, § 4.2, at 880 (acknowledging the advisability of weighing the expense and time required to engage in an extensive legal and factual inquiry versus the actual benefit of the opinion to the opinion recipient).

87. FitzGibbon & Glazer, *supra* note 76, at 872.

88. See ARIZ. REV. STAT. ANN. § 10-631(B) (2004).

may be verified by a review of the stock record book or by reliance on information provided by the corporation's transfer agent or corporate secretary. The opining lawyer should determine whether there has been an over-issuance of shares, because shares that are part of an over-issuance of shares are not duly authorized.

An opinion that shares are duly authorized, however, does not include an opinion that a proxy or other solicitation used in connection with a change in the authorized capital of the corporation was not false or misleading in some material respect. Therefore, the opining lawyer need not qualify the opinion regarding due authorization because of potential defects in proxy materials, unless the opining lawyer is aware of litigation or other specific circumstances that cast doubt on the validity of the change in authorized capital. The opinion is strictly limited to due authorization of the issuance of shares under corporate law.

c. Validity of Issuance

Shares are validly issued if: (1) they are duly authorized; (2) they were sold or otherwise transferred in compliance with applicable corporate law, the articles of incorporation of the corporation and its bylaws; (3) the corporation took all necessary corporate action to approve their issuance; (4) they were issued in accordance with such corporate action; and (5) share certificates were executed and delivered (or, for uncertificated shares, that applicable statutory requirements were met).

Arizona law generally does not impose special restrictions on the issuance of shares such as preemptive rights, unless the articles of incorporation provide otherwise. However, in the case of the issuance of shares as share dividends, shares may be distributed pro rata⁸⁹ and shares may not be distributed if: (1) the distribution would result in the corporation being unable to "pay its debts as they become due in the usual course of business"⁹⁰; or (2):

unless the articles of incorporation permit otherwise, the amount that would be needed, if the corporation were to be dissolved at the time of the distribution, to satisfy the preferential rights on dissolution of shareholders whose preferential rights are superior to those receiving the distribution.⁹¹

The opining lawyer should also confirm that there are no other restrictions imposed by law with regard to the issuance of shares. An example of

89. *Id.* § 10-623(A).

90. *Id.* § 10-640(C)(1).

91. *Id.* § 10-640(C).

another restriction that may apply arises in the context of professional corporations, which requires shareholders to be members of the profession.⁹² The articles of incorporation may also impose other restrictions on the issuance of shares such as a limitation on the issuance of a senior class of shares to an already-existing class of shares.⁹³

Under A.R.S. section 10-621, the directors of a corporation have the authority to issue shares in exchange for the receipt of valid consideration, although this power may be reserved to the shareholders under the articles.⁹⁴ After determining which body has the authority to issue shares, the opining lawyer should confirm that the shares were properly approved by the authorized body. The shares issued should be of the type or class of shares authorized to be issued and be in the number authorized in the relevant resolutions. The opining lawyer should also confirm by a review of the authorizing resolutions that there were no additional restrictions imposed on the issuance, such as the identification of the intended purchasers of the shares or a condition that shares would be issued only “on the receipt of subscriptions for a minimum number of shares.”⁹⁵ Finally, the resolutions must have been in full force and effect at the time of issuance.⁹⁶

The final aspect of determining the validity of the issuance of shares is that the corporation has taken all the steps required to vest shareholder status in the recipient of the shares.⁹⁷ Generally, the opining lawyer would confirm that share certificates were actually delivered and that the certificates were executed by an authorized officer of the corporation.⁹⁸ Shares may also be issued without certificates, in which case, the opining lawyer may confirm that a written statement that includes the information required under A.R.S. section 10-625 with regard to the form and content of share certificates was sent to the shareholder.⁹⁹

An opinion that shares are validly issued does not address whether the directors and officers issued the shares in compliance with their fiduciary duties.¹⁰⁰ It is possible for shares to be issued unfairly but still be validly issued.¹⁰¹ Whether shares are issued in compliance with directors’ and

92. *Id.* § 10-2220(A)(1).

93. *Id.* § 10-601.

94. *Id.* § 10-621.

95. FitzGibbon & Glazer, *supra* note 76, at 883–84.

96. *See* ARIZ. REV. STAT. ANN. § 10-602 (2004).

97. FitzGibbon & Glazer, *supra* note 76, at 884.

98. *Id.*

99. *See* ARIZ. REV. STAT. ANN. § 10-626 (2004).

100. *See* FitzGibbon & Glazer, *supra* note 76, at 877.

101. *See id.*

officers' fiduciary duties is a factual issue and a lawyer should not be required to give an opinion regarding the issue.¹⁰²

The opinion also does not address compliance with securities or other laws.¹⁰³ The validity of issuance of shares is not affected by a failure to comply with federal or Arizona securities laws. Failure to comply with such laws does not make share issuance void. Such defects may give the purchaser of the shares, and not any third parties, a right to rescind the purchase. Accordingly, an opinion regarding validity of issuance is not an opinion regarding compliance with federal or state securities laws or compliance with all requirements of law; instead, it only deals with the status of the shares under corporate law.

d. Assessability

Shares are “fully paid” if: (1) the consideration required by the resolutions authorizing or ratifying their issuance has been paid; and (2) such consideration was sufficient in kind and amount under the corporation's articles of incorporation and applicable law.¹⁰⁴ “Nonassessable” generally means that the shareholder cannot be assessed for further payments. In Arizona, “[w]hen the corporation receives the consideration for which the board of directors authorized the issuance of shares, the shares issued for the consideration are fully paid and nonassessable.”¹⁰⁵ Although the rule appears to be fairly straightforward, nothing in the statutes discusses or prohibits establishing assessable shares. Therefore, a corporation could have assessable shares, and the opining lawyer should review the articles of incorporation to confirm that there are no assessable shares with regard to any class or series of shares established by the corporation. Furthermore, there is an exception to the general assessability rule with regard to banking and insurance corporations, which are subject to the provisions of article XIV, section 11, of the Arizona Constitution.

In rendering an opinion that shares are fully paid and nonassessable, the opining lawyer should confirm two distinct issues: (1) that the consideration was in an amount and of the type allowed by statute; and (2) that such consideration was actually received.

102. *Id.*

103. *See id.* at 876.

104. ARIZ. REV. STAT. ANN. § 10-621(B)–(D) (2004).

105. *Id.* § 10-621(D).

The sufficiency of consideration is governed by A.R.S. section 10-621. The concept of “par value” has been abolished in Arizona¹⁰⁶ and, as a result, the concept of “watered stock” has also been eliminated.¹⁰⁷ Under section 10-621, shares may “be issued for consideration consisting of any tangible or intangible property or benefit to the corporation including cash, services performed, or other securities of the corporation”¹⁰⁸ (i.e. bonds, debentures, notes, other corporate obligations, or stock).¹⁰⁹ Future services of or promissory notes from the purchaser, however, do not constitute valid consideration.¹¹⁰ Shares may be issued for consideration in an amount deemed sufficient by the board of directors¹¹¹ and, in the absence of bad faith, this determination is conclusive with regard to the adequacy of consideration for purposes of establishing that shares are validly issued, fully paid, and nonassessable.¹¹²

Whether consideration was actually received by the corporation is a factual question. Therefore, reliance may be placed on an officer’s certificate by the opining lawyer. The opinion should state whether actual receipt of consideration was assumed, verified, or stated in the officer’s certificates.

In Arizona, under certain restrictions, shares may also be issued as dividends to a corporation’s shareholders pro rata without consideration, unless the articles of incorporation provide otherwise.¹¹³

The illustrative opinion addresses the validity and nonassessability only of the shares involved in the transaction. If the opinion includes prior issuances, the opining lawyer will be required to investigate all prior issuances or rely on opinions of other counsel.

106. Although the concept of par value has been abolished under the ABCA, nothing in the ABCA prohibits par value. Therefore, if a corporation chooses to include such provisions in its articles of incorporation it may do so. If the requested opinion pertains to a corporation that retains this concept, shares of such corporation must be issued for consideration not less than par value. *See* MODEL BUS. CORP. ACT § 6.21 cmt. n.1 (1999). The concept of par value also still exists with regard to shares issued by banking and insurance corporations. ARIZ. CONST. art XIV § 11. Article XIV, Section 11 of the Arizona Constitution may require that shares of such corporations have par value.

107. TERENCE W. THOMPSON, ET AL., ARIZONA CORPORATE PRACTICE § 5.6 (2003).

108. ARIZ. REV. STAT. ANN. § 10-621(B).

109. THOMPSON, *supra* note 107.

110. ARIZ. REV. STAT. ANN. § 10-621(B).

111. The board of directors has this power unless this power has been reserved to the shareholders by the articles of incorporation. *See* ARIZ. REV. STAT. ANN. § 10-621(A).

112. *Id.* § 10-621(C).

113. *See* ARIZ. REV. STAT. ANN. § 10-623(A) (2004).

e. Limited Liability Companies

Unlike corporations, limited liability companies (“LLCs”) “do not have rules concerning . . . discrimination within classes and series of [ownership] interests,”¹¹⁴ nor are there limitations on the number of authorized interests that may be issued by LLCs. There are default rules in the Arizona Limited Liability Company Act (“ALLCA”)¹¹⁵ that apply to the economic rights of members, but they are generally subject to the terms of the operating agreement of the LLC.¹¹⁶ Due to this flexibility, the concept of “due authorization” does not seem appropriate in the context of LLCs. If the LLC has an operating agreement, the preferences, limitations, and relative rights of the LLC interests will generally be set forth in the operating agreement and, if not, they would be subject to the default rules under the ALLCA.

Under section 29-701 of the ALLCA, “[a]n interest in [LLC] may be issued in exchange for a capital contribution or an enforceable promise to make a capital contribution in the future, or both.” The term “capital contribution” is defined in the ALLCA as “cash, other property, the use of property, services rendered or any other valuable consideration transferred to a limited liability company as consideration for issuing an interest in [an] [LLC].”¹¹⁷

Interests in an LLC are “validly issued” if they were sold or otherwise transferred in compliance with the ALLCA and the operating agreement. The ALLCA generally does not impose special restrictions on the issuance of LLC interests; however, the operating agreement may. Therefore, the opining lawyer should review the terms of the operating agreement and confirm that the interests were issued in compliance with it and that the LLC took all necessary LLC action to approve the issuance in accordance with the terms of the operating agreement. LLC action may be evidenced by member consents in some LLCs. Otherwise the opining lawyer may request and rely on a certificate of a member or manager, as applicable.

Although LLCs may issue certificates representing ownership interests, they are not so required under the ALLCA nor is this necessarily a common practice. Therefore, the concept of delivery does not generally seem to apply in the context of LLCs. If certificates representing ownership interests were issued, the opining lawyer can confirm that the certificates were

114. Robert R. Keatinge, et al., *The Limited Liability Company: A Study of the Emerging Entity*, 47 BUS. LAW. 378, 386 (1992).

115. ARIZ. REV. STAT. ANN. §§ 29-601 to -857 (2004).

116. *Id.* § 29-682.

117. *Id.* § 29-601(3).

executed and delivered by a properly authorized member¹¹⁸ (in a member-managed LLC) or manager of the LLC (in a manager-managed LLC). If certificates were not issued, the opining lawyer can confirm the membership and the ownership of interests in an LLC by a review of the articles of organization and the operating agreement, and all amendments thereto.

The terms “fully paid” and “non-assessable” are not used in the ALLCA. Generally, however, the amount and type of each member’s capital contribution and the date of the contribution will be set forth in the operating agreement for the LLC.¹¹⁹ Under the ALLCA, “the agreement or consent of all of the members is [required] to fix or modify the amount and character of the capital contributions that a member [is required] . . . to make in exchange for an interest in the [LLC],” unless the operating agreement provides otherwise.¹²⁰ If the LLC received a type of consideration allowed under the ALLCA and the amount received was approved by all of the members (as required under the ALLCA) or met the requirements set forth in the operating agreement, the interests should have been “fully paid and nonassessable,” but use of such terms in the LLC context does not seem to be appropriate.

Unlike in the corporate context where there are a number of procedural steps that are required in connection with proper capitalization, in the LLC context capitalization is essentially a contractual issue. As discussed in the previous paragraph, the members of an LLC determine the amount and type of consideration required for membership in the LLC. The task of the opining lawyer, therefore, is to confirm that each member did, in fact, make the contribution that was required in order to receive the membership interest. A review of the operating agreement, and any amendments thereto, should enable the opining lawyer to determine who are the members of the LLC. However, whether each member made the requisite capital contribution will not necessarily be evident by a review of the operating agreement. The problem of confirming the payment of consideration to the LLC may be further complicated if the operating agreement provides for additional capital contributions by members. To the extent additional capital contributions were required from the members, the operating agreement would not reflect this requisite, nor would the operating agreement indicate whether such contributions were actually paid by the members. The opining lawyer may be able to confirm the amount of total capital that was required

118. Generally each member of a member-managed LLC will have the authority to execute and deliver instruments on behalf of the LLC. *See* ARIZ. REV. STAT. ANN. § 29-654(A) (1998).

119. *See* 1 RICHARD C. ONSAGER, ARIZONA LIMITED LIABILITY COMPANY § 5.2.1 (1996 ed. Supp. 2003).

120. ARIZ. REV. STAT. ANN. § 29-701(B) (1998).

to be paid by the members if the LLC has copies of all notices for capital calls. However, whether consideration was actually received by the LLC is a factual question and, therefore, reliance on a certificate of the members or manager, as the case may be, would be appropriate. The opinion should state whether actual receipt of consideration was assumed, verified, or stated in such certificates.

An obligation of members to make additional capital contributions also raises another issue. Assuming all required capital contributions have been made by the members, the capitalization analysis does not end if the members have an ongoing obligation to make additional capital contributions as required by the LLC. In such a case, not only would the LLC membership interests be “assessable,” but depending on the terms of the operating agreement, members could be subject to dilution of their membership interests for failure to make such additional capital contributions or be subject to other remedies that may affect their membership rights.

Another issue particular to LLCs is the bifurcation of the economic rights and non-economic rights associated with a membership interest. Operating agreements often provide that if a member transfers a membership interest in an LLC, only the economic rights flow to the assignee unless and until the assignee is admitted as a member of the LLC. If the vesting of rights in a membership interest in an LLC is of particular concern in the transaction, this issue may be addressed and confirmed by the opining lawyer. Again, review of the operating agreement may or may not be sufficient to confirm the status of membership interests, and additional reliance on a certificate of members or managers may be appropriate.

Thus, an opinion regarding an LLC’s capitalization may provide as follows:

The Company has received all required capital contributions and there are no outstanding obligations of the members to make additional capital contributions to the Company.

3. Power and Authority; Due Authorization, Execution and Delivery

An opinion concerning corporate, limited liability company, or partnership power and authority rendered in connection with a transaction in which the subject entity is an Arizona corporation, limited liability company, general partnership, limited partnership, or limited liability partnership, generally addresses: (a) the power and authority of the entity to

conduct its business generally and to enter into the documents and to carry out the terms of those documents; (b) the action required on the part of the entity to authorize the transaction and to cause the documents to be executed and delivered; and (c) the execution and delivery of the documents.¹²¹

a. Power and Authority to Conduct Business and to Enter Into and Perform the Transaction

With respect to power and authority, the Illustrative Opinion provides:

The Company has the requisite corporate [limited liability company] [partnership] power and corporate [limited liability company] [partnership] authority to (i) own and operate its properties and assets [the properties and assets described in _____]; (ii) carry out its business as such business is currently being conducted [as described in _____]; and (iii) carry out the terms and conditions applicable to it under the Documents.

The above opinion means, with respect to an Arizona corporation, that the business activities of the corporation are not *ultra vires* and that the corporation's performance of its obligations under the transaction documents will not cause the corporation's activities to be *ultra vires*. It means, with respect to a limited liability company, general partnership, limited partnership, or limited liability partnership organized in Arizona, that the entity is legally authorized to conduct its business activities and to perform its obligations under the transaction documents.

The Committee recommends that, in giving this opinion, the phrase "corporate power and authority," "limited liability company power and authority," or "partnership power and authority" be used in order to emphasize that the opinion is based solely on a review of Arizona corporation, limited liability company, or partnership law and the entity's governing documents discussed below, and is not based on a broad review of Arizona, federal, and local authorizations and approvals.¹²² Nevertheless, the Committee recommends that all formulations of this opinion, including the phrases "power and authority," "requisite power and requisite authority," or "full power and full authority," be interpreted as having this same meaning.

The terms "power" and "authority" have traditionally been used in combination with the "requisite corporate power and corporate authority,"

121. See 1998 *TriBar Report*, *supra* note 1, § 1.2(a).

122. See *id.* § 4.1.

“requisite limited liability company power and limited liability company authority” and “requisite partnership power and partnership authority” opinions. The Committee believes that the words “power and authority” should not have separate meanings when used together in these opinions.

i) Corporations

With respect to corporations, this opinion may be substantiated by review of the corporation’s articles of incorporation, as amended, and bylaws. The powers granted to Arizona corporations under the Arizona Business Corporation Act are broad.¹²³ Accordingly, if the corporation’s articles of incorporation and bylaws do not restrict its corporate powers, this opinion should not be difficult to render under Arizona law.

Corporations that were in existence on the effective date of the Arizona Business Corporation Act may still be governed by articles of incorporation that were adopted under the more restrictive corporate law in effect prior to the effective date. If an opinion is requested about such a corporation’s power and authority, special attention should be paid to the corporation’s articles (for example, to debt limitation provisions) in light of A.R.S. section 10-1701.

ii) Limited Liability Companies

With respect to limited liability companies, this opinion may be substantiated by a review of the limited liability company’s articles of organization and operating agreement, each as amended. Under the ALLCA, limited liability companies have broad powers to engage in any lawful business or activity, except banking or insurance.¹²⁴

iii) Partnerships

With respect to partnerships, if the partnership is an Arizona general, limited, or limited liability partnership, this opinion may be substantiated by review of the applicable partnership agreement. Under both the Arizona Partnership Act and the Arizona Limited Partnership Act, partnerships have

123. The Arizona Business Corporation Act expressly provides that corporations may be organized for any lawful purpose which is not specifically prohibited under Arizona law. ARIZ. REV. STAT. ANN. § 10-301 (2004). See also ARIZ. CONST. art. XIV, § 4 (allowing corporations to have only those powers expressly granted by law or in their articles of incorporation).

124. ARIZ. REV. STAT. ANN. § 29-609(A) (1998 & Supp. 2005); *cf. id.* § 29-609 (indicating an LLC may conduct business as a title insurance agent as defined in the code).

broad powers to engage in business activities,¹²⁵ except that a limited partnership may not engage in the business of banking or insurance.¹²⁶

b. Due Authorization

With respect to due authorization, the Illustrative Opinion provides:

The execution, delivery, and performance of the Documents by the Company have been duly authorized by all requisite corporate [limited liability company] [partnership] action on the part of the Company.

This opinion means that any action or consent of: (i) the board of directors and/or shareholders of a corporation (as applicable); (ii) the members or managers of a limited liability company; or (iii) the general or limited partners of a partnership required to authorize the execution, delivery, or performance of the documents has been taken or obtained.

For a corporation, this opinion is often substantiated by a certificate of the corporate secretary about the due adoption of requisite resolutions. The opining lawyer may instead substantiate the opinion by examining the corporation's articles of incorporation, bylaws, minute books, and other appropriate records to ascertain, among other things, that: (i) the mailing of notices of meeting or meetings, if any, was timely; (ii) such notices were sent to the correct addresses; (iii) all waivers of notices were signed if notice was not given; (iv) the directors or shareholders (or both, if necessary) authorized the action; (v) a quorum was present at the time of the vote; (vi) the documents were properly submitted or summarized; (vii) the vote was sufficient; (viii) the officer executing the documents on behalf of the Company is authorized to do so; (ix) any directors authorizing the action were duly elected; (x) the meeting at which the action was authorized was duly convened and held; and (xi) all other required actions were properly taken. A third option is to obtain a satisfactory unanimous consent to action in lieu of meeting.

For a limited liability company, this opinion is often substantiated by obtaining a written consent of the members or managers, as the case may be, authorizing the requisite action. The opining lawyer may also substantiate the opinion by examining the limited liability company's articles of organization, operating agreement, company books, and other appropriate records to ascertain, among other things, that: (i) management of the Company is vested in the members or managers; (ii) the members or managers are authorized to execute and deliver documents on behalf of the

125. *Id.* § 29-206 (1998) (repealed 2000).

126. *Id.* § 29-306 (1998).

Company; (iii) the mailing of notices of meeting or meetings, if any, was timely; (iv) such notices were sent to the correct addresses; (v) all waivers of notices were signed if notice was not given; (vi) the members or managers (or both, if necessary) authorized the action; (vii) a quorum was present at the time of the vote; (viii) the documents were properly submitted or summarized; (ix) the vote was sufficient; (x) any managers authorizing the action were duly appointed or elected; (xi) any members authorizing the action were duly admitted; (xii) the meeting at which the action was authorized was duly convened and held; and (xiii) all other required actions were properly taken.

For a partnership, reference should be made to the partnership agreement to determine appropriate substantiation for this opinion.

The Committee recommends that in rendering this opinion, the phrase “duly authorized by all necessary corporate, limited liability company, or partnership action” be used in lieu of the phrase “duly authorized,” to emphasize that the opinion is based solely on a review of the entity’s records, and is not based on any consents or approvals of any governmental entity or other third party. Nevertheless, the Committee recommends that if the phrase “duly authorized” is used without modification, it be interpreted as having this same meaning.

c. Execution and Delivery

With respect to execution and delivery, the Illustrative Opinion provides:

[T]he Documents have been duly executed and delivered by the Company.

This opinion means that the officers, members, managers, or general partners who have signed the documents on behalf of the corporation, the limited liability company, or the partnership were authorized to do so, that their signatures were genuine, and that delivery has occurred.

If the entity is a corporation, this opinion may be based upon a resolution of the board of directors that authorizes the officers, either generally or by name, to sign the documents. If the entity is a limited liability company, this opinion may be based upon either (i) a resolution of the members that authorizes the members or managers, either generally or by name, to sign the documents, or (ii) a review of the articles of organization and the operating agreement to determine the members’ or managers’ authority to sign the documents. If the entity is a partnership, this opinion may be based upon a review of the applicable partnership agreement to determine the general partner’s authorization to sign the documents.

The opining lawyer should be present at the delivery of the documents, become satisfied in another manner that the delivery of the documents occurred, or assume delivery in the opinion.

4. Litigation and Other Alternative Dispute Resolution Proceedings

For many years opining lawyers have been required to provide only a “no litigation” statement in an opinion. With the increase in the use of alternative dispute resolution mechanisms, many recipients are requiring the traditional “no litigation” opinion to cover other forms of alternative dispute resolution, in addition to litigation.

The no litigation or alternative dispute resolution proceedings statement is actually a factual statement, more in the nature of a representation or confirmation than an opinion. The purpose of this statement is simply to give the recipient comfort that the opining lawyer does not possess any knowledge of pending or threatened legal proceedings. When this opinion is required, a statement such as the following is often used:

We have no knowledge of any [material] pending [or overtly threatened (in writing and delivered to opining lawyer)] litigation, arbitration, mediation, or other alternative dispute resolution proceeding against the Company that will negatively affect the transaction or that will have a materially adverse effect on the Company [except _____].¹²⁷

The Committee recommends that the phrase “overtly threatened” have the meaning provided in the ABA *Statement of Policy Regarding Lawyers’ Responses to Auditors’ Requests For Information*—A Report by the Committee on Auditors’ Inquiry Responses (amended 1990) (the “ABA Policy Statement”).¹²⁸ Thus, the phrase should mean, “that a potential claimant has manifested to the client an awareness of and present intention to assert a possible claim or assessment unless the likelihood of litigation (or, in the alternative, settlement) is considered remote.”¹²⁹

The opinion may limit the opining lawyer’s knowledge about overtly threatened action to a specific time period.

127. See discussion *infra* Part II.C. for use of the term “knowledge” and “material.”

128. Section of Corporation, Banking, and Business Law, American Bar Association, *Statement of Policy Regarding Lawyers’ Responses to Auditors’ Requests for Information*, 31 BUS. LAW. 565, 568 (Proposed Official Draft 1975).

129. *Id.*

The opining lawyer should avoid giving any opinion regarding the merits or the expected outcome of pending or threatened litigation, arbitration, or other alternative dispute resolution proceeding.¹³⁰

If an opinion is requested reflecting an examination in more depth than reflected in the definition of “knowledge,”¹³¹ with respect to pending litigation, the opining lawyer’s statement should include some description of the scope of independent verification efforts, if any. Possible alternatives include:

- (a) Based solely upon our knowledge and the representations of the Company [in the Agreement] [in an officer’s certificate delivered to us dated _____] . . .; or
- (b) Based solely upon [our examinations as of _____, _____, of the records of the filings in The Superior Court of _____ and United States District Court for the District of Arizona, [and _____] from _____, _____, through _____, _____, [our knowledge,] and the representations of the Company . . .; or
- (c) Based solely upon [our review of the results of the litigation search dated _____, _____ performed by _____] [our review of an Affidavit of the Clerk of the _____ County Superior Court/United States District Court for the District of Arizona]

If alternative (b) is used, limitations on the scope of the investigation should be clearly stated with respect to the date of examination and the jurisdictions and records searched. Alternative (c) should be used when the opining lawyer obtains litigation searches from a private search firm or affidavits from the clerks of the superior courts and U.S. District Court in Arizona. The opining lawyer should specifically limit the opinion with respect to pending litigation to those matters disclosed in the search results. As an alternative to the above approach of qualifying the opinion by identifying the specific examinations or searches conducted for purposes of the opinion, an opining lawyer may choose to include such examinations or searches in the definition of “knowledge” in another part of the opinion.

Because many of the alternative dispute resolution proceedings, including arbitration and mediation, are not the subjects of a court filing, independent verification of the existence or status of these types of proceedings may be difficult. Therefore, it is appropriate to request an officer’s certificate as to the existence or nature of such proceedings.

130. 1991 *Accord*, *supra* note 3, ¶ 17.5, at 214; *see infra* Part III.B.1.

131. *See infra* Part II.C.

5. No Consent or Approval

In certain transactions, an opining lawyer is asked to render an opinion that all consents or approvals of governmental entities necessary to allow the client to enter into and consummate the transaction, if any are required, have been obtained. The Illustrative Opinion provides:

No consent, approval, authorization, or other action by, or filing with, any federal, state, or local governmental authority is required in connection with the execution and delivery by the Company of the Documents and the consummation of the Transaction [or, if any of the foregoing is required, it has been obtained].

This opinion is frequently requested in corporate and securities transactions. By requesting this opinion, the recipient is seeking assurances that there has been no failure to obtain a regulatory approval that might otherwise render the client's obligations under the documents void or voidable, or the failure of which might subject the client to legal actions adversely affecting its business or ability to perform its obligations under the documents.

No "knowledge" limitation has been used in connection with this opinion because a limitation or disclaimer as to knowledge in an opinion primarily about legal rather than factual matters is generally inappropriate. Before giving the "no consent or approval" opinion, the opining lawyer should determine which governmental entities, if any, regulate the client's ability to enter into and consummate the transaction. It is appropriate for the opining lawyer to obtain an officer's certificate regarding the nature of the client's business and to limit the opinion to those matters disclosed in the officer's certificate.

The Illustrative Opinion includes an opinion only about consents or approvals necessary for the execution and delivery of the closing documents that are required to be obtained before or at the closing of the transaction. The phrase "consummation of the transaction" relates *only* to the transfer of consideration, the imposition of liens, the granting of assignments, or any other event which is a prerequisite to closing the transaction. A "no consent or approval" opinion as to the client's business operations or its performance of the transaction documents is generally overbroad and inappropriate and should not be given.

An opining lawyer may be asked to render an opinion about the "performance of the transactions required or contemplated" rather than the "consummation of the transaction." The Committee recommends that opinions be limited only to those approvals or consents necessary for the

closing of the transaction. If this “performance” opinion is required, the opining lawyer should also include a disclaimer of responsibility for advising the recipient of any changes in the regulation of the client’s business or any approvals or consents required in the future. The opining lawyer should also include an assumption that the client will obtain consents or approvals required in the future for the performance of its obligations.

6. Violation, Breach or Default

Traditionally, recipients have requested that opining lawyers render an opinion that the terms and conditions of the documents executed in connection with a transaction do not conflict with the requirements of organizational documents, agreements, judgments, orders, or decrees. The Committee believes that the term “conflict” is too imprecise. Accordingly, the Committee recommends that opining lawyers replace the “no conflicts” opinion with a “no violation, breach, or default” opinion. The “no violation” opinion is appropriate when referring to organizational documents, judgments, orders, decrees, or applicable law. The “no violation of applicable law” opinion is not intended to duplicate or supplement the enforceability opinion, but is intended to address only situations where Arizona law would render the documents void or voidable. The “no default or breach” opinion is appropriate when referring to agreements to which the client is subject (for example, this may include non-disparagement/non-compete agreements, franchise agreements, supply/sales agreements, patents or intellectual property, leases, loans, supply agreements, underwriting, and the like, etc.).¹³² The Illustrative Opinion provides:

(a) The execution and delivery of the Documents and consummation of the Transaction by the Company will not violate the Company’s [articles of incorporation] [articles or organization] [certificate of limited partnership], [bylaws] [operating agreement] [partnership agreement].

(b) [Based solely upon our knowledge,] The execution and delivery of the Documents and consummation of the Transaction by the Company will not violate any judgment, order, or decree of

132. However, the lawyer should not opine as to financial covenants or financial ratios in said agreements and the opinion should state:

We express no opinion, however, as to whether the execution and delivery of or the performance of the Company of its obligations under the Transaction will constitute a violation of, or default under, any financial covenant or financial ratios contained in any of the agreements referred to in the preceding sentence.

any court or governmental agency to which the Company is a party or by which it is bound.

(c) Based solely upon [our knowledge] [and a review of those material agreements disclosed to us by the Company on the [attached] officer's certificate dated _____, _____,] the execution and delivery of the Documents and consummation of the Transaction by the Company will not cause a breach or default of such material agreements.¹³³

An opining lawyer generally does not know the terms of every agreement to which the client is a party, or of every judgment, order, or decree affecting the client. Accordingly, it is appropriate for the opining lawyer to rely on an officer's certificate from the client stating that the client has disclosed all material or relevant agreements, judgments, orders, and decrees to the opining lawyer. The officer's certificate should specifically list the material or relevant agreements and the opining lawyer should review those agreements as part of the opining lawyer's due diligence activities prior to rendering the "no breach or default" opinion. In most cases, an opining lawyer may render an opinion that no violations exist with the client's articles of incorporation and bylaws [certificates of limited partnership and partnership agreements], or [articles of organization and operating agreement] without limiting the opinion to the opining lawyer's knowledge or reliance on an officer's certificate. One customary practice is for the officer's certificate to list the agreements to be reviewed by the opining lawyer and for the opining lawyer to interpret such agreements under Arizona law.

Because the due diligence required to give a full "no conflicts" opinion may be time-consuming and expensive, it is appropriate to tailor the scope of this opinion to the size and the needs of the transaction. The Committee therefore recommends that the parties and their respective lawyers consider whether a "no conflicts" opinion is needed and, if so, in what form. In addition, as discussed in the "no consent or approval" section above, the opining lawyer may also include an assumption that the client will obtain consents or approvals required in the future for the performance of its obligations.¹³⁴

A recipient may request an opinion that the execution and delivery of the documents and consummation of the transaction will not violate any applicable law, rule or regulation. This opinion overlaps with the

133. See discussion *infra* Part II.C. concerning the use and scope of the term "knowledge."

134. See *supra* Part II.B.5.

“enforceability” opinion¹³⁵ and the “no consent or approval” opinion¹³⁶ with respect to the execution and delivery of the documents and the consummation of the transaction. Therefore, if an “enforceability” or “no consent or approval” opinion is to be rendered, a “no conflict with laws, rules, or regulations” opinion may be redundant. Specifically, as will be discussed more fully below, the enforceability opinion generally provides that the documents are legal, valid, and binding obligations of the Company and are enforceable in accordance with their terms. To have a valid and enforceable document, the document generally cannot violate applicable laws. Similarly, rendering the “no consent or approval” opinion requires the opining lawyer to determine that the consummation of the transaction will not violate applicable laws, rules, or regulations requiring that such consent or approval be obtained.

To the extent that the parties are unable to obtain sufficient comfort through the “enforceability” and “no consent or approval” opinions, a “no violation with applicable laws, rules, or regulations” opinion may be appropriate. The Committee recommends the following form of opinion:

The execution and delivery of the Documents and consummation of the Transaction by the Company will not violate any applicable law, rule, or regulation affecting the Company.

Because this opinion calls for a purely legal conclusion the Committee recommends that the opining lawyer not limit the opinion to the lawyer’s knowledge.

A statement that the transaction will not violate any applicable law, rule or regulation refers only to the laws covered by the opinion, unless expressly stated otherwise.¹³⁷ The consensus of the Committee is that the term “applicable law” is limited to those laws and regulations that a lawyer exercising customary professional diligence would reasonably recognize as applicable in any material respect to the transaction contemplated by the documents, and does not include laws and regulations of county, municipal, and special political subdivisions, whether state, regional, municipal, or otherwise, unless expressly addressed in the opinion. While such exclusions are common practice, if an opining lawyer is aware of facts or circumstances that would materially alter the opinion if it were to include such matters, the opining lawyer may have an ethical obligation to either

135. *See infra* Part II.B.7.

136. *See supra* Part II.B.5.

137. *See supra* Part II.B.5.

disclose the issue with consent of the client, or to refrain from rendering the opinion.¹³⁸

Like the “no consent or approval” opinion and the “no violation of articles of incorporation, etc.” opinion discussed above, a “no violation of laws” opinion should be limited to the consummation of the transaction, and should not include future performance.¹³⁹ If a “performance” opinion is required, the opining lawyer may have difficulty in determining which of the applicable laws, rules or regulations might conflict with the performance obligations of the client in the contemplated transaction. To the extent possible, the scope of this inquiry should be decided when negotiating the form of the opinion. Depending on the circumstances of the transaction, the parties may agree to limit the scope of the “performance” opinion to include only specified laws.

The scope of the types of laws covered by the opinion may also be limited by the opinion itself, or in the concluding paragraphs of the opinion. For example, the limitations on the opinion may be stated:

Our engagement did not extend to, and we render no opinion about, any federal or state [insert bodies of law—e.g., tax, securities, environmental, public health, or labor laws, rules or regulations, zoning matters, or applicable building codes or ordinances] or the effect of such matters, if any, on the opinions expressed herein.

7. Enforceability of Documents

a. The Scope of the Enforceability Opinion

Most opinions (except those limited by the recipient to organization, existence, and authority of an entity) will include an “enforceability”¹⁴⁰ or “remedies”¹⁴¹ opinion. At the time of the 1989 Report, the “standard litany”¹⁴² typically read:

138. See generally *infra* Part IV.

139. See *supra* Part II.B.5 (discussing consummation versus performance).

140. See, e.g., DONALD W. GLAZER ET AL., GLAZER AND FITZGIBBON ON LEGAL OPINIONS § 9.1 (2d ed. 2001); AM. COLL. OF REAL ESTATE LAWYERS ATTORNEYS’ OPINION COMM. & AM. BAR ASS’N SECTION OF REAL PROP., PROBATE AND TRUST LAW COMM. ON LEGAL OPINIONS IN REAL ESTATE TRANSACTIONS, *Real Estate Opinion Letter Guidelines*, 38 REAL PROP. PROB. & TR. J. 241, § 4.0-4.0.d (2003), available at <http://www.abanet.org/rppt/cmtes/rp/i5/final-opinion-2003.pdf> [hereinafter *ACREL/ABA Guidelines*].

141. See 2003 *TriBar RA9 Report*, *supra* note 1, at 1460–61; 1998 *TriBar Report*, *supra* note 1, § 3.1, at 619–21; 1991 *Accord*, *supra* note 3, § 10, at 198–201.

142. GLAZER ET AL., *supra* note 140, § 9.1, at 206 n.9.

The Documents constitute legal, valid, and binding obligations of the Company, enforceable in accordance with their terms.

Since that time, enforceability opinion language has undergone considerable scrutiny and seemingly endless discussion. It has been characterized and criticized as being inherently redundant.¹⁴³ While attempts have been made to justify¹⁴⁴ or explain¹⁴⁵ the meaning and use of each of these terms, there is an emerging trend to drop the word “legal,”¹⁴⁶ and there is support to eliminate the phrase “in accordance with their terms” (or similar language) as being “implicit”¹⁴⁷ or adding nothing to the intended meaning.¹⁴⁸ The attempt of the Accord, however, to reduce the mantra simply to “enforceable”¹⁴⁹ has not prevailed, and some combination of the words “valid,” “binding,” and “enforceable” is commonly requested by opinion recipients. The revised Illustrative Opinion provides:

The Documents are valid, binding, and enforceable obligations of the Company.

If the recipient insists, however, the inclusion of the phrase “in accordance with their terms” (or similar phrasing) or the addition of the word “legal” should not provide an Arizona opining lawyer cause for substantial concern.

Arizona lawyers continue to consider the collective words “legal,” “valid,” “binding,” and “enforceable” to be interchangeable and, with or without the phrase “in accordance with their terms,” to have a single

143. See ASS'N OF THE BAR OF THE CITY OF N.Y., COMM. ON REAL PROP. LAW, ATTORNEY OPINION LETTERS COMM., REAL PROP. LAW SECTION, SUBCOMMITTEE ON MORTGAGE LOAN OPINIONS & THE N.Y. STATE BAR ASS'N, *Mortgage Loan Opinion Report*, 54 BUS. LAW. 119, 151 (1998) [hereinafter *NY Mortgage Report*].

144. See James J. Fuld, *Legal Opinions in Business Transactions: An Attempt to Bring Some Order Out of Some Chaos*, 28 BUS. LAW. 915, 928–29, 931 (1973).

145. See, e.g., Johannes K. Gäbel & Roland F. Fürst, *Legal Opinions on Corporate Matters*, in LEGAL OPINION LETTERS: A COMPREHENSIVE GUIDE TO OPINION LETTER PRACTICE §§ 3.12–.16, at 3-53 to -70 (M. John Sterba, Jr., ed., 3d ed. 2003).

146. See, e.g., TASK FORCE ON FORMS UNDER REVISED ARTICLE 9, UNIF. COMMERCIAL CODE COMM., FORMS UNDER REVISED ARTICLE 9, at 256 (Jonathan C. Lipson ed., 2002) (Form 5.2.1); GLAZER ET AL., *supra* note 140, § 9.1, at 206 n.9; *Id.* § 9.6, at 256 (“At one time the word ‘legal’ also was included . . . Today, it ordinarily is not.”); JOINT ABA/ACREL COMM., INCLUSIVE REAL ESTATE SECURED TRANSACTION OPINION, para. 2.4 <http://www.acrel.org/documents/publicdocuments/inclusiverealestatesecuredtransactionopinion.htm> (last visited Mar. 19, 2006) [hereinafter INCLUSIVE OPINION]; see also 1998 *TriBar Report*, *supra* note 1, § 3.1, at 619 (noting that the omission of “legal” fails to “expand[] or limit[] the generally understood meaning of the remedies opinion”).

147. 1991 *Accord*, *supra* note 3, § 10, cmt. ¶ 10.1.

148. See GLAZER ET AL., *supra* note 140, § 9.1, at 207 n.10, § 9.6, at 232 n.3; 1998 *TriBar Report*, *supra* note 1, § 3.1, at 619–20.

149. See 1991 *Accord*, *supra* note 3, § 10, cmt. ¶ 10.1.

meaning.¹⁵⁰ Whatever the particular form, for Arizona opining lawyers and recipients of their opinions, the enforceability opinion should be understood to include and mean:

- (1) The documents constitute effective contracts under applicable law, and none of them is invalid by reason of a statute, rule, reported court decision, or “public policy;”
- (2) Absolute contractual defenses to the documents, such as the statute of frauds, are not available to the subject entity;
- (3) The documents are sufficient to create the interests, rights, and obligations they purport to create; and
- (4) Except to the extent otherwise qualified in the opinion, each term and provision of the documents is binding upon the subject entity and the remedies expressly provided for therein will be enforced by a court against the subject entity.¹⁵¹

Inherent in any enforceability opinion are the implicit conclusions of the opining lawyer (unless otherwise stated as assumptions or express qualifications) that the subject entity is properly formed and validly exists with the entity power and authority to enter into such obligations, and that it has duly authorized the execution, delivery, and performance of the same.¹⁵²

150. See generally GLAZER ET AL., *supra* note 140, § 9.1, at 207 n.10 (pointing out that California lawyers are in agreement with this consensus that, no matter which words or phrases are included or excluded, “that no different meaning should be given to these different forms of remedies opinions.”); 1998 *TriBar Report*, *supra* note 1, § 3.1, at 619 (“The remedies opinion may take a number of forms without any difference in meaning.”); AD HOC COMM. OF THE BUS. LAW SECTION WASH. STATE BAR ASS’N, REPORT ON THIRD-PARTY LEGAL OPINION PRACTICE IN THE STATE OF WASHINGTON, 27–29 n.33 (1998), <http://www.wsba.org/lawyers/groups/businesslaw/opinionreport.doc> (last visited Feb. 2, 2006) [hereinafter WASHINGTON REPORT]. There is, therefore, “bi-coastal” support for the Arizona position in this regard. This may also serve as an example of what the RESTATEMENT (THIRD), *supra* note 1, calls “customary practice.” *Id.* § 95 cmt. c; see also *id.* § 51 cmt. e; *id.* § 95 Rep. Note to cmts. b-c; 1998 *TriBar Report*, *supra* note 1, § 1.4, at 600–03.

151. For other formulations, each of which uses different phrasing, but all of which are intended to establish essentially the same meaning for the enforceability opinion, see 1991 *Accord*, *supra* note 3, § 10, at 198–99; INCLUSIVE OPINION, *supra* note 146, ¶ 2.4 (“[T]he Transaction Documents form a contract; a remedy will be available with respect to each agreement of the Client in the Transaction Documents or such agreement will otherwise be given effect; and any remedy expressly provided for in the Transaction Documents will be given effect as stated.”); 1998 *TriBar Report*, *supra* note 1, § 3.1, at 620; WASHINGTON REPORT, *supra* note 150, at 27 n.33 (“[W]hatever the phraseology, . . . the obligations are legally binding on the corporation.”).

152. 1991 *Accord*, *supra* note 3, § 10, cmt. ¶ 10.4, at 200; WASHINGTON REPORT, *supra* note 150, at 28 n.33 (“[i]t [is not] necessary to include . . . building block opinions within the body of the opinion letter.”).

*b. Common Exceptions and Limitations*¹⁵³

An enforceability opinion is almost always given subject to certain exceptions or qualifications, particularly in recognition that subsequent events, such as bankruptcy, can impair the enforceability of previously agreed-upon documents, no matter how phrased, and that certain provisions in those documents may be unenforceable under particular facts and circumstances or because of matters of public policy.¹⁵⁴ Three commonly accepted general exceptions or qualifications to enforceability include:

i) Bankruptcy-Insolvency

The first general exception is the “bankruptcy-insolvency-creditors’ rights” exception. The Illustrative Opinion provides:

The enforceability of the Documents may be subject to or limited by bankruptcy, insolvency, reorganization, arrangement, moratorium, and other similar laws relating to or affecting the rights of creditors generally.

While it has been asserted that this exception is implicit and need not be stated,¹⁵⁵ this exception customarily is included in opinions by Arizona lawyers, and the Committee recommends its continued inclusion in any opinion addressing document enforceability.

For Arizona opining lawyers and recipients of their opinions, this exception should be read expansively and be understood to include:

the Federal Bankruptcy Code, and thus includes (by way of specific examples) matters of turn-over, automatic stay, avoiding powers, federal fraudulent transfer, preferences, discharge, conversion of a non-recourse obligation into a recourse claim or the reverse, limitations on *ipso facto* and anti-assignment or due-on-sale or transfer clauses, “cash-collateral” treatment, and the coverage of pre-petition security agreements and collateral assignments to post-petition assets;

153. An enforceability opinion will normally not include that a non-compete provision is not enforceable.

154. See 1998 *TriBar Report*, *supra* note 1, §§ 3.3–.5, at 622–30; 1991 *Accord*, *supra* note 3, §§ 11–14, at 202–06; WASHINGTON REPORT, *supra* note 150, 35–37 nn.47–48 & 52; see also 2002 *Guidelines*, *supra* note 1, § 4.8, at 881 (“Because public policy is a principal basis for invalidating contractual provisions, opinion givers should not qualify their opinions as a whole with a general exception for ‘matters of public policy.’”). *But see* 2002 *Guidelines*, *supra* note 1, at 875 n.6.

155. GLAZER ET AL., *supra* note 140, § 9.10.1, at 265 n.2; 1998 *TriBar Report*, *supra* note 1, § 3.3.1, at 623; 1991 *Accord*, *supra* note 3, §§ 11–12, at 202–04.

all other federal and state bankruptcy, insolvency, reorganization, equity, or other requested receivership, moratorium, and arrangement procedures or proceedings, and assignments for the benefit of creditors, all of which affect the rights and remedies of creditors generally (not just creditors of specific types of debtors);

all of the foregoing matters that affect or refer to particular creditors of specific types of debtors, such as financial institutions and insurance companies;

state fraudulent conveyance and fraudulent transfer laws, inclusive of their application in bankruptcy-insolvency matters; and

judicially developed doctrines in this area, such as substantive consolidation of entities and equitable subordination.¹⁵⁶

The relative terseness of this exception is not intended to exclude specific and more detailed treatment of a particular “bankruptcy-insolvency-creditors’ rights” issue in an opinion. If the particular facts of a transaction could give rise to a specific issue,¹⁵⁷ then the recipient or its counsel may request that an opinion specifically address such an area of concern, or the opining lawyer may want to address such a perceived issue by a specifically targeted opinion as well.

Some Arizona lawyers previously have expressed concern that, because this exception as phrased above refers only to “enforceability,” it does not qualify the opinion about “validity.” They believe, for example, that the limitation for “bankruptcy” may be insufficient to disclose the potential vulnerability in bankruptcy of a guarantee of payment, a deed of trust or other conveyance on a fraudulent conveyance/transfer or preferential transfer theory. This concern, however, is inconsistent with the Arizona practice of reading “valid,” “binding,” and “enforceable”¹⁵⁸ collectively and interchangeably. Therefore, the Committee recommends that this (and every) exception to the enforceability opinion be read as applying collectively to the words “valid,” “binding,” and “enforceable.”

Although more typically posed in the context of the “general limitation” exception discussed below, some Arizona lawyers have expressed concern

156. Largely taken from 1991 *Accord*, *supra* note 3, § 12, at 202–03, and INCLUSIVE OPINION, *supra* note 146, ¶ 3.3.

157. Such as a claim of fraudulent transfer or conveyance, as where collateral is provided by a corporation other than the borrowing entity; because of particular timing issues in a loan or workout situation, there is the heightened potential for a preference claim in any bankruptcy; or in a situation where there is potential for a “substantive consolidation” of a debtor and related entities closely involved or affected by a particular transaction.

158. And “legal,” if its inclusion is insisted upon by the recipient.

based on the apparent paradox posed by the fact that most opinions state or are understood to “speak only as to the date they are issued,” but that these stated exceptions largely concern events that will take place in the future.¹⁵⁹ However, virtually all “bankruptcy-insolvency-creditors’ rights” are “forward looking,”¹⁶⁰ in that they have effect, if any, only in instances of future enforceability of contractual provisions, and then only under the particular facts and circumstances that have evolved and exist at that point in time. This concern does not seem to be a proper reason to avoid addressing these possible exception matters at the time an enforceability opinion is rendered.

ii) Equitable Principles

The second common exception is the “equitable principles” exception.¹⁶¹ The Illustrative Opinion provides that:

The enforceability of the Documents is subject to general principles of equity.

This exception likewise commonly appears in Arizona opinions. The Committee recommends its continued inclusion, preferably stated separately as provided in the Illustrative Opinion, or alternatively as an addition to the bankruptcy-insolvency-creditors’ rights exception, although doing so intermingles related but separate concepts. Some opinion recipients request the addition of a phrase such as, “regardless of whether enforceability is considered in a proceeding in equity or at law.” Because of the merger of law and equity in Arizona,¹⁶² this addition is unnecessary.

For Arizona opining lawyers and recipients of their opinions, this exception should be read and understood to include principles:

(a) governing the availability of specific performance, injunctive relief, or other equitable consideration of the impracticability or impossibility of performance at the time of particular remedies, which generally place the award of such remedies, subject to certain guidelines, in the discretion of the court to which application for such relief is made;

159. Except for specialized “debtor-in-possession” transactions such as “DIP financing,” presumably there is—at the time of closing—no bankruptcy or insolvency pending or known to be threatened.

160. See 1998 *TriBar Report*, *supra* note 1, § 1.2(f), at 598–99.

161. For examples that combine this exception with the bankruptcy-insolvency exception, see 1998 *TriBar Report*, *supra* note 1, at 668 & n.191; WASHINGTON REPORT, *supra* note 150, app. Illustrative Opinion ¶ D-1, n.47.

162. ARIZ. R. CIV. P. 1, 2 (2005).

- (b) affording equitable defenses (*e.g.*, waiver, laches, and estoppel) against a party seeking enforcement;
- (c) requiring good faith and fair dealing in the performance and enforcement of a contract by the party seeking its enforcement;
- (d) requiring reasonableness in the performance and enforcement of an agreement by the party seeking enforcement of the contract;
- (e) requiring consideration of the materiality of (i) [one party's] breach and (ii) the consequences of the breach to the party seeking enforcement;
- (f) requiring consideration of the impracticability of performance at the time of attempted enforcement, and;
- (g) affording defenses based upon the unconscionability of the enforcing party's conduct after the parties have entered into the contract.¹⁶³

Again, virtually all of these principles are also “forward looking” in nature and will have effect, if at all, only in the future.¹⁶⁴ Finally, this equitable principles exception now customarily applies to the opinion as a whole, and should not be deemed limited solely to the enforceability opinion paragraph.¹⁶⁵

iii) General Limitation

Although less prevalent at the time of the 1989 Report, opinions now typically include a “general” or “generic” limitation. Its basis is succinctly stated: “As a result of dissatisfaction with [a] laundry list approach, many lawyers have searched for an easier, more comprehensive, method of narrowing the scope of the remedies opinion while at the same time providing adequate assurance to the opinion recipient.”¹⁶⁶

The revised Illustrative Opinion provides:

Enforceability of the Documents is subject to qualification that certain waivers, procedures, remedies, and other provisions of the Documents may be unenforceable under or limited by the law of

163. 1991 *Accord*, *supra* note 3, § 13, at 204; *see* INCLUSIVE OPINION, *supra* note 146, ¶ 3.4.

164. One report observes that, “If before rendering the remedies opinion the opinion preparers believe that coercion, duress or similar inequitable conduct has prevented the formation of the agreement in question, they should not render the opinion (or should disclose their concerns, if the client consents).” 1998 *TriBar Report*, *supra* note 1, § 3.3.4, at 625 n.77.

165. *See* GLAZER, *supra* note 140, § 9.9, at 261–64; 1998 *TriBar Report*, *supra* note 1, § 1.2(c), at 597–98.

166. *NY Mortgage Report*, *supra* note 143, at 156.

the State of Arizona; however, such possible unenforceability or limitations will not render the Documents invalid as a whole or substantially prevent the practical realization of the principal benefits [or security] intended by the Documents (except for the economic consequences of procedural or other delay).¹⁶⁷

This generic exception recognizes that, although certain specific provisions of an agreement may not be enforceable, either as a matter of conflict with specific Arizona statutes or common law decisions,¹⁶⁸ or under particular facts and circumstances (especially taking account of the equities or public policy matters),¹⁶⁹ a party may nevertheless pursue recognized legal remedies, enforce essential terms of the documents, and generally achieve the intended purposes of the agreement. Use of this exception should eliminate the need for more specific qualifications (the “laundry list”).¹⁷⁰ The language of this limitation, however, has not been the subject of a definitive court decision in Arizona (or elsewhere, to the Committee’s knowledge) and is not free from ambiguity.¹⁷¹ Although the meaning of the phrase “practical realization of the benefits intended by the documents” may depend upon the custom and practice in the particular type of transaction, the exception includes the implicit assumption that the party enforcing its remedies will do so in a commercially reasonable manner consistent with, and as limited by, applicable law.

167. *Infra* app. A, Part IV.c. For more specific exceptions, see *infra* Parts II.B.8.(c) (Guaranties), II.B.8.(e) (UCC Security Interests), II.B.8.(g) (Intellectual Property), II.B.8.(h) (Bankruptcy Remote Entities).

168. See *infra* Part II.B.8.(f) (Real Estate Liens); see also ARIZ. REV. STAT. ANN. §§ 33-722 (2000) (electing between action on debt or action to foreclose); ARIZ. REV. STAT. ANN. § 12-1566 (2000) (imposing certain “fair market value” limitations on deficiency claims); ARIZ. REV. STAT. ANN. § 33-813 (Supp. 2005) (granting statutory right of reinstatement in certain circumstances, notwithstanding prior acceleration of debt upon a default); Gary Outdoor Advert. v. Sun Lodge, Inc., 650 P.2d 1222 (Ariz. 1982) (attempting to waive statutes of limitations in documents in advance of any actual accrual of a cause of action); Elson Dev. Co. v. Arizona Sav. & Loan Ass’n, 407 P.2d 930 (Ariz. 1965) (attempting to waive statutory rights of redemption in advance of any default and foreclosure in documentation); Ross v. Ross, 393 P.2d 933 (Ariz. 1964).

169. See *Arizona Coffee Shops, Inc., v. Phoenix Downtown Parking Ass’n*, 387 P.2d 801 (Ariz. 1963) (finding that unconscionable or bad faith actions may deny right of acceleration even after a default); *Ciavarelli v. Zimmerman*, 593 P.2d 697 (Ariz. Ct. App. 1979) (stating that general course of conduct may render attempted exercise of remedies unconscionable).

170. See GLAZER ET AL., *supra* note 140, § 9.11, 275–78; Robert A. Thompson, *Opinions in Real Estate Transactions*, in LEGAL OPINION LETTERS, *supra* note 145, § 5-1, 5-32 to -45; 1998 *TriBar Report*, *supra* note 1, § 3.4, at 626–27; WASHINGTON REPORT, *supra* note 150, at n.52; cf. 1991 *Accord*, *supra* note 3, § 11, cmt. ¶ 11.2, at 202.

171. See ACREL/ABA *Guidelines*, *supra* note 140, §§ 4.0-4.0.a, at 9; NY *Mortgage Report*, *supra* note 143, at 156–58; Thompson, *supra* note 170, § 5.11, at 5-39 to -40; 1998 *TriBar Report*, *supra* note 1, § 3.4.1, at 626–27.

For example, loan documents often contain provisions, such as statute of limitations waivers, or absolute election of simultaneous remedies, that are of questionable enforceability in Arizona.¹⁷² But the unenforceability of certain provisions does not mean that the documents have not created an obligation to pay the debt, to act upon a collateral assignment, or to create a valid real property lien. Even if certain particular provisions are unenforceable, the exception is appropriate if the documents are nonetheless sufficient to permit the lender to pursue recognized legal remedies to enforce payment of the debt, including acceleration of the indebtedness in the event of a material breach of a material covenant or obligation. In the case of loan documents creating liens or security interests, such remedies are foreclosure, trustee's sale, and UCC public or private dispositions or strict foreclosure, as appropriate. In the case of a promissory note, one remedy is an action to enforce the debt. The qualification should not be read, however, to provide assurance to the lender about the borrower's financial ability to satisfy the debt, or that the debt actually will be paid when due. Further, the reference to practical realization does not provide assurance that the realization of the benefits of the transaction will not be affected by delays caused by, for example, bankruptcy or injunctive relief, or by laws unrelated to the enforceability of the documents, such as general moratoria or public emergency laws.

Although the generic exception/principal benefits qualification is intended to avoid the need to list numerous specific qualifications, opining lawyers may nevertheless wish to comment on provisions about which they have a particular concern, even if the unenforceability of those provisions would not prevent the practical realization of the intended benefits. In light of the uncertainty inherent in the concept of "materiality,"¹⁷³ lawyers may consider calling attention to specific provisions of questionable enforceability when the provisions are unusual or when it is apparent from the negotiations that such provisions are of special importance in the transaction.

If the documents contain provisions that may be unenforceable and the unenforceability of those provisions would substantially prevent the practical realization of the benefits intended by the documents, the general limitation will not suffice. In those instances, the potentially unenforceable provisions should be the subject of specific exceptions or limitations, as discussed below.

172. See *supra* note 168.

173. See 2002 *Guidelines*, *supra* note 1, § 3.2, at 878 ("When possible, an opinion giver should avoid use of a materiality standard by using objective criteria . . . when limiting the matters addressed by an opinion.").

The language used in the general limitation may vary from the form stated above. For example, one variation eliminates the word “practical” but includes “principal” before the word “benefits.” Slight differences in the formulation of this general limitation should not alter its purpose or meaning. Some lawyers add something like the following additional language to the general limitation referred to above, “except for the economic consequences of any procedural delay that may result from such laws.” This additional language highlights the fact that the intervention of Arizona or federal law may cost time and money, so that a party’s economic interests are affected adversely. In a lending transaction, for example, even if a deed of trust by its terms provides that real property may be sold by the trustee ten days following a notice of election to sell, the lender nevertheless will be subject to the longer statutory notice and timing requirements of Arizona statutes dealing with the trustee’s power of sale. Other examples would be delay caused by bankruptcy or temporary or preliminary injunctive relief. The addition of such language should not be read to narrow or expand the basic concept of the general limitation itself, and is not absolutely necessary.

Lawyers representing out-of-state recipients, or who are themselves unfamiliar with the laws of Arizona, periodically may request a specific listing of the waivers, procedures, remedies, and other provisions that may be unenforceable. The preparation of such an exhaustive listing is contrary to Arizona opinion custom and practice and is appropriate only where the scope of the transaction merits the required time and due diligence.¹⁷⁴ Doing so may also violate the “golden rule” if it is not usual or customary for the lawyer requesting such a “laundry list” opinion to render the same under similar circumstances.¹⁷⁵

8. Typical Enforceability Issues

Particular areas of law present common problems in connection with an enforceability opinion, and are frequently the subject of separate opinion requests (or in transactions involving so-called “special purpose entities”—separate opinions) by recipients or their lawyers. These include the following topics, which are, to a greater or lesser extent, subsumed in an enforceability opinion.

174. *Id.* § 1.2, at 876.

175. *Id.* § 3.1, at 878.

a. *Usury*

Questions arise with respect to usury issues in financing transactions. Absent a specific disclaimer by the opining lawyer, the general enforceability opinion should be understood implicitly to *include* “usury” within its scope.¹⁷⁶ The opining lawyer should therefore evaluate the legality of the particular transaction terms under the usury laws.¹⁷⁷ Frequently, recipients will request a separately stated “usury opinion.” In either circumstance, under Arizona’s “any rate of interest agreed to by the Borrower” general interest laws,¹⁷⁸ this should not be problematic for an Arizona opining lawyer. The “catch-22” built into such law (if the borrowing party is required to pay or pays the lending party amounts that exceed the “agreed upon rate of interest”—such as paying “side fees” not governed by any written agreement or sums later re-characterized by a court to be “interest” even though not denominated as such—then arguably the usury penalty statutes¹⁷⁹ may have been violated¹⁸⁰) however, should be avoided.¹⁸¹ The Committee recommends that the opining lawyer include in any opinion dealing with enforceability, as well as any opinion addressing usury separately, a stated assumption to the effect that the lender “will receive no interest, charges, fees, or other benefits or compensation in the nature of interest in connection with the transaction other than those that the Company has agreed in writing in the documents to pay” (or any comparable qualification). If the “chosen law” that will govern usury is not that of Arizona, then in opinions limited by their terms to Arizona law, usury will not be addressed by implication in any enforceability opinion. In any event, by following the *Restatement (Second) of Conflict of Laws (1971)* Section 203, Arizona has adopted the more liberal “substantial

176. See 1998 *TriBar Report*, *supra* note 1, § 3.5.2 (a)(iii), (c), at 628–30; ACREL/ABA *Guidelines*, *supra* note 140, § 4.0.b, at 10; NY *Mortgage Report*, *supra* note 143, at 153–54. See generally Thompson, *supra* note 170, § 5.13, at 5-47 to 5-51.

177. See, e.g., *Layne v. Transamerica Fin. Servs., Inc.*, 707 P.2d 963 (Ariz. Ct. App. 1985).

178. See ARIZ. REV. STAT. ANN. §§ 44-1201 to -1207 (2003).

179. See *id.* §§ 44-1202 to -1204.

180. This concern is not as far-fetched as it might seem to be at first glance. At least two courts have concluded that it may be possible to commit usury in Arizona if a lender charges a borrower more than its written agreement otherwise permits. *S&N Equip. Co. v. Casa Grande Cotton Fin. Co.*, 97 F.3d 337, 341–43 (9th Cir. 1996); *Wieman v. Roysden*, 802 P.2d 432, 436–37 (Ariz. Ct. App. 1990).

181. This is handled frequently by including somewhere in the pertinent documents signed by the party to be charged, typically in a promissory note or loan agreement, language whereby the party agrees to pay the rate of interest that is stated or that results from the inclusion of any fees or charges that are deemed to be in the nature of interest, all of which that party agrees in any event to pay to the lending party.

relationship” test to sustain or validate a contract against a charge of usury.¹⁸²

b. Choice of Arizona Law

An opining lawyer will generally have to address choice of law or governing law issues either by implication¹⁸³ or expressly upon request by the opinion recipient or its counsel. How an opining lawyer addresses choice of law depends upon what governing law is selected by the transaction documents.¹⁸⁴

Unlike some jurisdictions, Arizona has not adopted statutes having general application to contract choice of law issues.¹⁸⁵ As to choice of law principles, the Arizona appellate courts since 1968—virtually without exception—have cited and followed the *Restatement (Second) of Conflict of Laws (1971)* in resolving choice of law issues or conflict of law questions.¹⁸⁶ This includes following Sections 187 (party autonomy—parties choose applicable law in their contract) and 188 (contacts to determine and follow in absence of express choice of law in a contract), as well as other more specialized Sections such as 203 (validation against usury under law of any state having “substantial relationship” to parties and transaction, a more liberal standard than that of state of “most significant relationship”) and 229 (law governing repayment of indebtedness, not law governing deed of trust or mortgage securing that indebtedness, will govern post-foreclosure deficiency rights and claims). With the adoption of Revised Article 9 of the UCC, Arizona now has express and detailed statutory provisions dealing

182. *Burr v. Renewal Guar. Corp.*, 468 P.2d 576, 577 (Ariz. 1970).

183. *See infra* text preceding note 186.

184. *See infra* text accompanying notes 185–203.

185. *See* CAL. CIV. CODE § 1646.5 (West 1985); DEL. CODE ANN. tit. 6, § 2708 (2006); 735 ILL. COMP. STAT. 105/5-5 (2003); LA. CIV. CODE ANN. art. 3540 (1994); N.Y. GEN. OBLIG. LAW §§ 5-1401 to -1402 (McKinney 2001); OHIO REV. CODE ANN. § 2307.39 (West 2004); TEX. BUS. & COM. CODE ANN. § 35.51 (Vernon 2002).

186. *See* RESTATEMENT (FIRST) CONFLICTS OF LAW decisions, including *Schwartz v. Schwartz*, 447 P.2d 254 (Ariz. 1968), *overruled on other grounds by Fernandez v. Romo*, 646 P.2d 878 (Ariz. 1982); *W. Coal & Mining Co. v. Hilvert*, 160 P.2d 331 (Ariz. 1945); *Smith v. Normart*, 75 P.2d 38 (Ariz. 1938).

The only decision that clearly has balked at following the RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971) has been *Brandler v. Manuel Trevizo Hay Co.*, 740 P.2d 958 (Ariz. Ct. App. 1987), which seemingly ventured into “modern interest analysis” because of unhappiness with the apparent result otherwise dictated by then-applicable Sections 142 and 143 of the RESTATEMENT (SECOND) OF CONFLICT OF LAWS. This decision may be treated as aberrational, particularly because effective the following year, 1988, Section 142 was extensively re-written and Section 143 was deleted. As re-drafted, Section 142 probably would have led to a result consistent with the *Brandler* decision.

with choice of law matters in the context of security interests in personal property and fixtures.¹⁸⁷

If the transaction documents contain provisions that choose a particular governing law to control the interpretation, construction, and enforcement of those documents and the transaction, Arizona customary practice has followed the view that, absent an express exclusion or qualification by the opining lawyer or the inclusion of a specific “choice of law opinion,” a general enforceability or remedies opinion incorporates an implicit opinion that the governing law provision(s) will be given effect under the choice of law rules applied by Arizona courts. Since this conclusion in most instances is based on an application of *Restatement (Second) of Conflict of Laws (1971)* Section 187 principles, including its built-in “exceptions,” any Arizona opinion addressing enforceability of documents that contain an express choice of law provision should contain the following stated assumption (or its equivalent):¹⁸⁸

[t]he result of any application of Arizona law as specified in the Documents will not be contrary to a fundamental policy of the law of any other state with which the parties may have material or relevant contact in connection with the Transaction, and as to which there is a materially greater interest in determining an issue of choice of law.¹⁸⁹

187. See ARIZ. REV. STAT. ANN. § 47-1105(A) (2005) (following law chosen by the parties bearing a “reasonable relation” to the chosen state; and absent an express choice of law, applying the law of the state bearing an “appropriate relation” to the transaction); see also *id.* §§ 47-9301 to -9307 (special Revised Article 9 rules). See generally *infra* Part II.B.8.e (discussing UCC Security Interests).

188. This assumption also should be included in any opinion letter that contains a separate, express choice of law opinion.

189. See generally *Swanson v. Image Bank, Inc.*, 43 P.3d 174 (Ariz. Ct. App. 2002). Notwithstanding an express choice in the employment agreement to apply Texas law, the court, citing the RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(b), refused to exclude the recovery claim by the discharged employee under Arizona’s wages and treble damages law, ARIZ. REV. STAT. ANN. §§ 23-350 to -355 (2005) (no Texas counterpart). *Swanson*, 43 P.3d at 185. The Court concluded that Arizona had the most significant relationship to the transaction and the parties, and that application of Arizona treble damage remedies law—*respecting the remedies issue*—represented a fundamental interest and policy of Arizona that would not be defeated by the choice of Texas law in the agreement. *Id.* at 185–86; see also *Landi v. Arkules*, 835 P.2d 458, 462–63 (Ariz. Ct. App. 1992) (negating express choice of Illinois law in “heir finder” agreement by the application of RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)).

To clarify the reason for this assumption for the recipient or its counsel (at least in a proposed form of the opinion letter), it may be helpful to include these citations, without the summaries, at the end of the assumption or in a footnote. This particular assumption does not address the other qualification that the chosen law has “no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties’ choice . . .” because the

The opinion recipient may also request a separate “choice of law opinion.”¹⁹⁰ Because the general choice of law rules governing Arizona contracts arise through the common law, the opining lawyer should give a reasoned opinion. The revised Illustrative Opinion provides several alternatives.

A concise opinion could read (with or without citations):

Based upon decisions of the Supreme Court of Arizona and applicable Arizona statutes, we believe the courts in Arizona will honor the choice of law clause(s) in the Documents. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS, Sections 187, 188, 203 and 229, comment e (1971); *Cardon v. Cotton Lane Holdings, Inc.*, 173 Ariz. 203, 205–09, 841 P.2d 198 (1992); *Burr v. Renewal Guar. Corp.*, 105 Ariz. 549, 550, 468 P.2d 576, 577 (1970); ARIZ. REV. STAT. sections 47-1105(A) and 47-9301 to -9307, inclusive (U.C.C. RA9).

A longer exposition that incorporates all of Restatement section 187 could read:

You have requested that we advise you whether an Arizona court would give effect to the choice of law provision in the Documents in favor of the law of the State of _____. The Supreme Court of Arizona has consistently ruled that where it is not bound by a previous decision or by legislative enactment, it will follow the rules in the *Restatement (Second) Of Conflict Of Laws (1971)*, including, without limitation, the Restatements of Conflict of Laws. *Smith v. Normart*, 51 Ariz. 134, 75 P.2d 38 (1938); *W. Coal & Mining Co. v. Hilvert*, 63 Ariz. 171, 160 P.2d 331 (1945); *Burr v. Renewal Guar. Corp.*, 105 Ariz. 549, 468 P.2d 576 (1970); *Cardon v. Cotton Lane Holdings, Inc.*, 173 Ariz. 203, 841 P.2d 198 (1992); *Taylor v. Sec. Nat’l Bank*, 20 Ariz. App. 504, 514 P.2d 257 (1973); and *In re Levine*, 145 Ariz. 185, 700 P.2d 883 (Ariz. Ct. App. 1985). Section 187 of the *Restatement (Second) Of Conflict Of Laws* provides that the parties to a contract may stipulate their choice of law to govern the contract and that the laws of the state chosen will be applied unless (i) the particular

presence or absence of these factors should be patently obvious to the opining lawyer. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(a) (1971). If the purportedly chosen law has no apparent basis for inclusion in the documentation, either that choice should be changed or the opining lawyer should expressly exclude choice of law from any opinion letter.

190. Even if not separately requested, when there is an enforceability opinion being provided, an opining lawyer may wish to incorporate the “reasoned basis” for such an opinion under Arizona law by including a separate choice of law opinion paragraph.

issue is one that the parties could not have resolved by an explicit provision in their agreement directed to that issue and (ii) either:

The chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or

Application of the law of the chosen state would be contrary to a fundamental policy of a state that has a materially greater interest than the chosen state in the determination of the particular issue and that, under the rule of Section 188 of the *Restatement (Second) Conflict of Laws*, would be the state of applicable law in the absence of an effective choice of law by the parties.

Based on the facts concerning the negotiation of the Documents, [such as the place of negotiation and execution of the Documents being the State of _____] and the terms thereof and considering such other matters as we have deemed relevant, we believe that an Arizona court would give effect to the choice of law provisions in the Documents in favor of the law of the State of _____, (subject to the application of Arizona law with respect to the enforcement of rights and remedies against [real] property located in Arizona).

Generally, the transaction documents will choose Arizona law to govern the transaction documents or will choose foreign law to govern all or part of the transaction documents. If the documents choose Arizona law to govern the transaction documents, this choice would be consistent with the jurisdictional limitation of the law being addressed by the opining lawyer.¹⁹¹ In this case, unless there are unusual circumstances present that cast doubt on the “substantial relationship” of Arizona law to the parties and the transaction in question,¹⁹² the Arizona opining lawyer should be willing to render an enforceability opinion, with or without a separate opinion expressly addressing choice of law,¹⁹³ while including the qualification stated above.¹⁹⁴ This means that the opining lawyer has made a professional judgment that the courts of Arizona will apply Arizona “substantive law” to the parties’ agreement and enforce that agreement under Arizona law (as qualified and limited elsewhere in the opinion).¹⁹⁵

191. See *supra* Part II.A.2 and *infra* Part III.C.

192. See *supra* note 187.

193. See *supra* note 186 and accompanying text.

194. See *supra* notes 181–83 and accompanying text.

195. See, e.g., *supra* Part II.B.7.b (discussing common exceptions and limitations in enforceability opinions).

If the documents state that the law of a jurisdiction other than Arizona (“foreign law”) will govern all or part of the transaction documents,¹⁹⁶ three alternatives are: (1) the recipient may be satisfied with a limited opinion addressing the likelihood that an Arizona court will enforce the choice of foreign law as provided in the documents;¹⁹⁷ (2) the opining lawyer does not provide an enforceability opinion; or (3) the opining lawyer limits the enforceability opinion to only those documents—or aspects of documents—that select Arizona law to control.

Notwithstanding the predominant choice of foreign law as governing the documents and the transaction, recipients nevertheless may want to receive a general enforceability opinion. In this situation, the opining lawyer needs to determine which of several possible responses is *actually* desired by the recipient.

One response is to retain an additional lawyer in the chosen-law jurisdiction to provide the enforceability opinion based on the law of that state.¹⁹⁸ This may be disfavored because of the additional expense and added complexity of obtaining another opinion.

A second response¹⁹⁹ is to discuss what would happen if a court were to disregard the specific choice of law provision in the documents and to apply Arizona law.²⁰⁰ As an example of this approach, the opinion may state:

The Documents indicate that they are to be governed by the laws of the State of _____. We have no knowledge of those laws

196. *See, e.g.*, *Cardon v. Cotton Lane Holdings, Inc.*, 841 P.2d 198, 203–04 (Ariz. 1992) (lender was denied any deficiency by application of California’s strict “one form of action” and anti-deficiency laws when parties chose California law to control their loan agreement and promissory note and Arizona law to govern the deed of trust).

197. *See supra* Part II.A.2.

198. *See* 1998 *TriBar Report*, *supra* note 1, § 4.6, at 635–36.

199. *E.g.*, 1991 *Accord*, *supra* note 3, § 10(b), (d), cmt. ¶ 10.5, at 198–201; *see also* GLAZER, *supra* note 140, § 9.12.3, at 283–91; 1998 *TriBar Report*, *supra* note 1, § 4.6, at 635–36; Laurence G. Preble, *Choice of Law Opinions: Making the Right Choice*, *PROB. & PROP.*, July-Aug. 1997, at 13, 13.

200. Opining lawyers may address the choice of law issue by assuming that the laws of the jurisdiction in the choice of law provision are the same as those of Arizona. One example is language that resembles the following:

Certain of the Documents state that they are to be governed by _____ law. We disclaim familiarity with _____ law and render no opinion about it. For purposes of the opinions set forth in this letter, we have assumed, with your consent, that _____ law is identical in all relevant respect to the laws of the State. We express no opinion about the reasonableness of this assumption.

This approach is commonly used, and the result of this qualification appears to be roughly equivalent to the suggestions contained in this Report. The Committee, however, does not favor use of this approach because it requires a patently false assumption, namely, that the laws of the chosen jurisdiction are the same as the laws of Arizona.

and express no opinion thereon. Whichever law is ultimately determined to apply to the Documents, however, if the Documents were governed by Arizona law, then our opinions set forth above would remain unchanged.

The opining lawyer would then typically include a standard enforceability opinion.²⁰¹ This approach requires the opining lawyer to examine the documents in question as though they would be controlled by and enforced under Arizona law (presumably pointing out any contrary or questionable provisions), and should provide the recipient with some comfort that if a court were to refuse to honor the specific choice of law provision in the documents and apply Arizona law instead, the documents would nevertheless be enforceable under Arizona law.²⁰² This approach may also include a separate opinion that the Arizona courts likely will enforce the choice of law provisions as discussed above.²⁰³

Finally, an opining lawyer may decline to provide any enforceability opinion as to foreign-law-controlled documents, or may exclude choice of law issues from the opinion entirely. This type of response may not be accepted by the recipient. Given the number of different possible responses, it seems best to address these issues directly and early in the transaction with the recipient and its counsel, to avoid a “false start” in the opinion drafting process, misunderstandings, or disagreements on the eve of closing.

An opining lawyer may be faced with transaction documents that are silent as to governing law. Any choice of law opinion in that situation would be difficult because of the number of essentially factual matters that could bear on controlling law under the “most significant relationship” principles expressed in *Restatement (Second) of Conflict of Laws (1971)* Section 188: place of contracting; place of negotiation; place of performance; location of “subject matter” of the contract; and the domicile, residence, nationality, place of incorporation/organization, and place of business of the parties. Although probably not implicit in an enforceability opinion (since the documents have no applicable provision addressing this issue), a recipient could request a choice of applicable law opinion in these circumstances. In such a case, the opining lawyer is best served by insisting on the inclusion of an express choice of law provision in each significant document, or by declining to render any such opinion because it requires too much factual analysis and weighted judgments of relative significance

201. See *supra* Part II.B.7.

202. See GLAZER, *supra* note 140, § 9.12.3, at 284–85; 1998 *TriBar Report*, *supra* note 1, § 4.6, at 635–36; Preble, *supra* note 199, at 13–14.

203. See *supra* note 190 and accompanying text.

of such facts. In any event, any choice of law opinion in this situation is outside normal, customary practice in Arizona.

c. Guaranties

In addition to the types of guaranties which are commonly recognized, there are many obligations undertaken or assumed by persons, including pledges of property, for the debts of another which can be classified as guaranties.²⁰⁴ This identification of guaranties is particularly important since in Arizona a guaranty is not enforceable against the marital community of a husband and wife unless both join in the guaranty.²⁰⁵ The opining lawyer should carefully analyze each transaction to determine whether guaranties exist which should be addressed in the opinion. For example, there may be occasions when a practitioner is presented with a guaranty document drafted by counsel not familiar with A.R.S. section 25-214. The guaranty, as presented, sets forth a single name of a married person and Arizona counsel is asked to opine regarding the enforceability of the instrument. Given the requirement of Arizona law for both spouses to join in transactions of guaranty, suretyship, or indemnity in order to bind the marital community, opining counsel is faced with at least three choices. Initially, counsel should discuss the matter with the client and make the client aware of the statute and its effect on the proposed transaction. After discussion, counsel can suggest that the matter be raised directly between counsel, that the client raise the matter directly with the opposing party's representative, or that opining counsel advise drafting counsel that the document be executed solely in the name of the single named spouse, dealing with his or her sole and separate property. If none of those three alternatives is acceptable to the client, opining counsel should consider that rendering an opinion regarding such a document without making the opinion recipient aware of the provisions of A.R.S. section 25-214 may be misleading. Another possible solution may be to modify the opinion language so that it accurately reflects the nature of the guaranty, for example:

The guarantee as drafted is enforceable against the signer's sole and separate property, but is not enforceable against the marital community or the community property [pursuant to A.R.S. section 25-214].

The enforceability of a guaranty is dependent upon the actual language of the guaranty, the type of guaranty involved, and the facts involved in a particular case, so that the opining lawyer should carefully consider all such

204. See RESTATEMENT (THIRD) OF SURETYSHIP & GUAR. § 1 (1996).

205. ARIZ. REV. STAT. ANN. § 25-214(C)(2) (2000).

factors. See, for example, the discussion under Bankruptcy-Insolvency in Part II.B.7.b.i, where fraudulent transfer issues may be involved in guaranties by entities of the debt of another, including guaranties by subsidiaries of parent's debt or "sister" entity's debt. With respect to payment guaranties, there may be limitations on the enforcement of such guaranties after a deed of trust sale of property owned by the principal debtor or property given by the guarantor to secure payment under the guaranty.²⁰⁶ Guaranties of completion create additional potential problems with respect to the enforceability of a requirement that a guarantor physically complete a structure after a trustee's sale has occurred with respect to the property because of the statutory requirement to establish a deficiency.²⁰⁷

Another area of concern is that an enforceability opinion is often requested about a guaranty that purports to waive in advance some or all of the legal protections traditionally granted to sureties and guarantors. Examples of such protections are found in Arizona statutes²⁰⁸ and Arizona rules of procedure,²⁰⁹ as well as common law. Some protections apparently may be waived in advance²¹⁰ and some apparently may not.²¹¹ Arizona courts construe attempts at such waivers in favor of the guarantor.²¹² The

206. See ARIZ. REV. STAT. ANN. §§ 12-1566, 33-727, 33-814 (2000 & 2003).

207. See *id.* § 33-814.

208. See *id.* §§ 12-1641 to -1646, 47-9102(A)(28), 47-9610 (2005).

209. See ARIZ. R. CIV. P. 17(f).

210. See *United States v. Crain*, 589 F.2d 996, 1001 (9th Cir. 1979) (finding that language in a standard loan guaranty agreement waived protection afforded by statute); *Maestro Music, Inc. v. Rudolph Wurlitzer Co.*, 354 P.2d 266, 274 (Ariz. 1960) (finding that a buyer may validly waive statutory resale provisions with an agreement entered into after default and which is supported by consideration); *McClellan Mortgage Co. v. Storey*, 704 P.2d 826, 829-30 (Ariz. Ct. App. 1985) (finding that the defense provided for by statute had been waived); see also U.C.C. § 3-605 cmt. 2 (2002) (discharging of a party to an instrument if there is, among other things, unjustifiable impairment of security without the consent of the guarantor). *But see Data Sales Co. v. Diamond Z Mfg.*, 74 P.3d 268, 272-74 (Ariz. Ct. App. 2003) (supporting the holding of binding waivers with a broad reading and application of the RESTATEMENT (THIRD) OF SURETYSHIP & GUAR. §§ 41, 48 (1996)).

211. For example, the rights to receive notice of disposition of and to redeem collateral cannot ordinarily be waived in advance. ARIZ. REV. STAT. ANN. § 47-9624 (2005). These protections may extend to guarantors since a guarantor may be a "debtor" as defined in A.R.S. section 47-9102(A)(28). *Int'l Harvester Co. v. Fuoss*, 758 P.2d 649, 651 (Ariz. Ct. App. 1988); see also *Gary Outdoor Adver. Co. v. Sun Lodge, Inc.*, 650 P.2d 1222, 1223-24 (Ariz. 1982) (stating that advance waivers of statutes of limitation are against public policy); *Data Sales Co.*, 74 P.3d at 272-74.

212. See, e.g., *D.W. Jaquays & Co. v. First Sec. Bank*, 419 P.2d 85, 89 (Ariz. 1966) (stating that guarantor may waive his equitable rights of subrogation and right to discharge for release, impairment, or exchange of security, but only "by the most unequivocal language in the guaranty agreement"). *But see Data Sales Co.*, 74 P.3d at 272-74.

full extent of limitations on such waivers has not been finally determined by the supreme court under Arizona law.²¹³

Although the general limitation that certain waivers, procedures, remedies, and other provisions may be unenforceable under or limited by the law of Arizona applies to the provisions and waivers often found in guaranties, a lawyer should be cautious about using the “practical realization” opinion with respect to guaranties that contain such provisions or waivers. If particular provisions or waivers are not enforceable, then action by the beneficiary of the guaranty in reliance upon the provision or waiver may not result in any realization of the benefits intended by the guaranty. The effect of such action could be the full release or discharge of the guarantor.²¹⁴ If the guarantor is released or discharged, then the beneficiary will receive no benefits under the guaranty.

In the opinion, a lawyer may use a variety of ways to resolve the issues raised in the context of guaranties when the “practical realization” opinion is added to the general limitation that certain waivers, procedures, remedies, and other provisions may be unenforceable or limited by Arizona law. Two possible approaches are discussed below. One is to exclude the guaranty from the “practical realization” opinion by adding the phrase “other than the Guaranty” to the end of that opinion. The effect of doing so is to exclude from the enforceability opinion any opinion with respect to those waivers, procedures, remedies, and other provisions in the guaranty that are subject to limitations contained in Arizona law generally. The other approach, which the Committee believes is most commonly used by Arizona lawyers, is to add a phrase such as the following: “except that the application of principles of guaranty and suretyship to the acts or omissions of the Lender after execution and delivery of the Guaranty may prevent the practical realization of the benefits intended by the Guaranty through a release or discharge of a guarantor.” The effect of this approach is to limit the exceptions to the “practical realization” opinion to exceptions for Arizona law of guaranty and suretyship only. The Illustrative Opinion includes these two approaches as examples of alternatives:

213. Courts in other jurisdictions have recognized limitations. *See, e.g.*, *United States v. Willis*, 593 F.2d 247, 255–56 (6th Cir. 1979) (citing cases allowing defense of commercial reasonableness).

214. *See W. Sur. Co. v. Horrall*, 533 P.2d 543, 544 (Ariz. 1975); *Indian Vill. Shopping Ctr. Inv. Co. v. Kroeger Co.*, 854 P.2d 155, 158 (Ariz. Ct. App. 1993); *Int'l Harvester*, 758 P.2d at 650–52; *Scottsdale Disc. Corp. v. O'Brien*, 543 P.2d 158, 161–63 (Ariz. Ct. App. 1975). *But see Data Sales Co.*, 74 P.3d at 272–74; RESTATEMENT (THIRD) OF SURETYSHIP & GUAR. ch. 3, topic 3, tit. B, introductory note (1996) (“[T]his Title discharges a secondary obligor to the extent that such acts would otherwise cause the secondary obligor to suffer a loss; in some cases, the discharge is total.”).

Enforceability of the Documents is further subject to the qualification that certain waivers, procedures, remedies, and other provisions of the Documents may be unenforceable under or limited by the law of the State of Arizona; however, such law does not in our opinion, substantially prevent the practical realization of the benefits intended by the Documents [other than the Guaranty] [except that the application of principles of guaranty and suretyship to the acts or omissions of the Lender after execution and delivery of the Guaranty may prevent the practical realization of the benefits intended by the Guaranty through a release or discharge of a guarantor.].

By including the above alternatives in the Illustrative Opinion, the Committee does not intend to recommend one alternative over the other or to exclude other approaches to the issue. Other approaches exclude guaranties from the documents declared to be enforceable or discuss the limitations inherent in the law of guaranty and suretyship. A third alternative is to limit particular provisions of the guaranty “to the extent permitted by law.” Also, if the size of the transaction merits the required time and due diligence, the opining lawyer may justifiably be asked to give an opinion discussing the specifically enforceable or unenforceable provisions in a guaranty. As discussed above, any opinion should be negotiated as early in the transaction as possible; this is particularly true of opinions about guaranties because of the special issues involved.

d. Indemnification Clauses

Despite the regular inclusion of indemnification provisions in various types of transaction documents such as stock or asset sale agreements, securities underwriting and placement agreements, and investment banking engagement letters, courts have relied on precepts of public policy to limit their enforceability when the party seeking indemnification has been found liable for negligence, gross negligence, or intentional misconduct. When indemnity language does not specifically address the effect of the indemnitee’s negligence, the indemnity agreement is generally construed to permit indemnification for a loss that results in part from an indemnitee’s passive negligence, but not for a loss that results from an indemnitee’s active negligence. If the effect of the indemnitee’s negligence is addressed in the agreement, then the agreement must clearly and unequivocally specify the result desired by the parties.²¹⁵ Because the indemnity agreement may be less than unequivocally clear, or because the intent of the agreement

215. See *Cunningham v. Goettl Air Conditioning, Inc.*, 980 P.2d 489, 493 (Ariz. 1999).

may hinge on the post-agreement conduct of a party, an opinion on an indemnity clause requires special care. Indemnity provisions are often strictly interpreted against the party purportedly entitled to such contractual indemnification. In addition, the Securities Exchange Commission is of the view that indemnification of directors, officers, and controlling persons for liability arising under the Securities Act of 1933 is against public policy as expressed in the Securities Act of 1933 and is therefore unenforceable (Regulation S-K, Item 510). Accordingly, given the legal uncertainties arising from the application of public policy and/or the future actions of the party seeking indemnification, it is common practice in some types of agreements to either expressly: (a) exclude indemnification provisions from enforceability opinions or (b) indicate that the opinion is subject to the effect of:

generally applicable rules of law that limit the enforceability of provisions releasing, exculpating, or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction, to the extent the action or inaction involves negligence, gross negligence, recklessness, willful misconduct, or unlawful conduct, or where such provisions would violate public policy.

In some cases, however, such broad exclusions will not be possible and the indemnity language will have to be analyzed for enforceability under prevailing case law. An alternative is to re-draft the indemnity clause so that it applies “to the maximum extent permitted by law.” Such self-limiting language provides assurances to the indemnitee while limiting coverage to indemnification that would be enforceable under prevailing law, thereby eliminating the risk of an incorrect opinion.

e. Special Issues – UCC Security Interests

Since the 1989 Report was issued, Revised Article 9 (“RA9”) of the UCC has been adopted in all states, the District of Columbia and the U.S. Virgin Islands, in most cases with an effective date of July 1, 2001. RA9 has changed or elaborated upon a number of basic rules with respect to the creation and perfection of security interests in personal property, most notably in the classification of types of collateral and the place of filing financing statements. Because RA9 has been in effect in Arizona since July 1, 2001, this Report assumes that the opinion being requested relates to a transaction occurring after that date. If the transaction has elements that occurred prior to July 1, 2001, the opining lawyer should consult the RA9

transition rules before rendering an opinion on either creation or perfection of a security interest.

i) Creation of Security Interest

The UCC states the choice of law rules that apply to transactions covered by RA9. With respect to creation of security interests, general contract provisions and the creation, attachment, and enforcement of security agreements are governed by the law selected by the parties (so-called “party autonomy”)—*provided* the transaction bears a reasonable relation to the jurisdiction so selected.²¹⁶ Absent such an express choice of law in the documents, apparently the version of the UCC adopted by the state bearing an appropriate relation to the transaction will control.²¹⁷

Consistent with the scope of a typical enforceability or remedies opinion,²¹⁸ and absent any express exclusions of security interests entirely, an enforceability opinion should be understood to include an implicit opinion about the *creation*²¹⁹ of a security interest in personal property whenever the subject documents purport to create a security agreement.²²⁰ As in other instances,²²¹ this should be understood by the opining lawyer and the recipient to mean that the security agreement is sufficient to create, as a contract, an enforceable agreement and set of undertakings,²²² namely, that the security document contains sufficient operative language and terms

216. See ARIZ. REV. STAT. ANN. § 47-1105(A) (2005). This statute is comparable, but not identical to the RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1971), discussed *supra* text accompanying notes 186–90. If recent amendments to U.C.C. § 1-105 are adopted in Arizona, then these provisions will be brought much closer in line with this Restatement.

217. See ARIZ. REV. STAT. ANN. § 47-1105(A). Again, this statute is comparable, but not identical to the principles of the RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 6, 188; *cf.* Cardon v. Cotton Lane Holdings, Inc., 841 P.2d 198, 203 (Ariz. 1992) (“A court usually applies the ‘local law of the state selected by application of the rule of § 188’ to determine whether the parties could have resolved a particular issue by explicit agreement.”) (citing RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. c).

218. See *supra* Part II.B.7.a.

219. Although “created” or “creation” are not defined terms, they are used throughout Revised Article 9. See, e.g., ARIZ. REV. STAT. ANN. § 47-9102(A)(72) (“‘Security agreement’ means an agreement that creates or provides for a security interest.”); U.C.C. §§ 9-201 cmt. 2, 9-203 cmt. 2 (2000). *But see* 2003 *TriBar RA9 Report*, *supra* note 1, at 1461 n.41 (excluding “creation” as well as “attachment” from a “remedies opinion cover[ing] the enforceability of the security agreement as a contract.”).

220. The collateral may or may not include fixtures. The security interest may be part of a deed of trust or realty mortgage, part of a loan or credit agreement, or may be found in one or more separate security agreements.

221. See *supra* Part II.B.8.a (Usury), Part II.B.8.b (Express choice-of-law provisions).

222. See GLAZER, *supra* note 140, § 12.2, 410–13; 2003 *TriBar RA9 Report*, *supra* note 1, at 1463–64.

to create or provide for a security interest, that there is a sufficient and adequate description of RA9-covered collateral therein, and that any express choice of Arizona law is effective (reasonable relationship to Arizona).²²³

An enforceability opinion (absent explicit treatment) should *not* be deemed inherently to address and include Article 9 security interest issues of attachment, perfection, or priority of security interests.²²⁴ Furthermore, any general limitation exception to enforceability in the opinion²²⁵ must be understood to include the myriad qualifications, special rules, and exceptions that are—inherently—a part of the UCC, especially RA9. To clarify that any opinion dealing with one or more security interests is intended to include what the *TriBar Revised Article 9 Report* calls the “U.C.C. Scope Limitations,”²²⁶ the Illustrative Opinion includes a summary of the same as an assumption:

Our opinion as to fixtures and personal property cover only (i) security interests created under Chapter 9 (Revised Article 9) of the Arizona UCC, (ii) UCC collateral or transactions, and (iii) UCC perfection methods [that are limited to filing a financing statement].

Notwithstanding the inclusion of the creation of security interests in any general enforceability opinion, many recipients continue to request more specific separate opinions about the form and consequences of security interests. Stopping short of Article 9 opinions, the revised Illustrative Opinion provides:

The [security agreement document] is sufficient to create²²⁷ in favor of the Lender a security interest in any rights of the Company in the described collateral in which a security interest can be created under Article 9 of the Uniform Commercial Code (“UCC”).

223. See *supra* notes 216–17.

224. See ARIZ. REV. STAT. ANN. §§ 47-9203(A), 47-9301 to -9342 (2005); GLAZER, *supra* note 140, § 12.2, 412–13, §§ 12.3–12.8; 2003 *TriBar RA9 Report*, *supra* note 1, at 1454–55, 1463, 1465–66.

225. See *supra* text accompanying notes 164–71.

226. See 2003 *TriBar RA9 Report*, *supra* note 1, at 1457–59.

227. See GLAZER, *supra* note 140, § 12.2, 411–12, for a discussion of the perceived distinctions between and nuances of “create” versus “sufficient to create.”

ii) Attachment, Perfection, and Priority

a) Attachment

In many transactions, there is little or no need in an express opinion to address the complexities posed under RA9 by attachment, perfection, or priority. As to attachment, two of the three necessary elements are essentially factual in nature (debtor has rights in, or the right to encumber, the collateral in question) or under the control of the secured party/recipient (value has been given),²²⁸ and it is common for an opinion giver to assume the existence of both those matters in any opinion. This leaves the existence of an authenticated record sufficient as a security agreement—which is subsumed elsewhere in opinions given on execution, authorization, delivery, and enforceability (creation), and so it seems unnecessary to address attachment separately or expressly.

b) Perfection

If there are one or more financing statements included in the documents subject to the enforceability opinion,²²⁹ then a general enforceability opinion probably should be understood to mean that the same is or are in appropriate Arizona form for filing in this jurisdiction,²³⁰ and has or have been completed with sufficient information to function as a financing statement under Arizona's RA9.²³¹ Except that the UCC1 form is appropriate to create perfection if the facts set forth in the form are accurate, this should *not* (absent explicit treatment) be deemed to include or address

228. ARIZ. REV. STAT. ANN. § 47-9203(B).

229. Because financing statements no longer need be signed or authenticated by a debtor, and may be prepared and filed by the secured party with little or no involvement of the debtor (leaving aside the question whether a financing statement itself can ever be enforceable), some Arizona opining lawyers have excluded financing statements from the documents covered by their general enforceability opinions, electing to deal with them in a separate, express opinion paragraph, much like guaranties. See Ad Hoc Committee on Third-Party Legal Opinions of the Business Law Section of the Washington State Bar Association, *Supplemental Report on Third-Party Legal Opinion Practice in the State of Washington Covering Secured Lending Transactions* (Oct. 2000), available at <http://www.wsba.org/lawyers/groups/businesslaw/supplementalreport3rdparty2000.doc> (last visited Apr. 6, 2006), reprinted in GLAZER, *supra* note 140, app. 22-A; NY *Mortgage Report*, *supra* note 143, at 129, 163–65 & n.41.

230. See ARIZ. REV. STAT. ANN. §§ 47-9502(C), 9521. This does not, however, imply that Arizona is necessarily the proper location for filing the same or that this is the correct or best form for this particular transaction.

231. The UCC1 forms are sufficient under A.R.S. section 47-9502(A) (debtor's name, secured party name, some adequate description of collateral that includes therein the collateral in the security agreement) and are non-rejectable by the Arizona filing offices under sections 47-9516(B) and 9520(A).

issues of attachment, perfection, or priority, and not to imply any opinion as to the applicable law (or laws) regarding perfection, the effect of perfection or non-perfection, and priority.²³²

The fixture financing statement [or the deed of trust, or both] is [are] in proper form for filing with the office of the county recorder and, upon due filing in such office, will constitute a “fixture filing” under the UCC with respect to any fixtures described therein. The central financing statement is in proper Arizona form for filing with the office of the Arizona Secretary of State and, upon due filing in such office, will perfect a security interest in that collateral described therein as to which a security interest has been duly granted to Lender by the Company and to the extent a security interest can be perfected in such collateral under the Arizona UCC by the filing of a financing statement in the office of the Arizona Secretary of State.

This opinion assumes that the debtor is an Arizona registered organization or its equivalent; that any fixtures are located in Arizona; that there is at least some personal property subject to RA9 described sufficiently first in a security agreement and then in the central filing financing statement; that the same may be perfected properly by a central filing in Arizona; that the debtor has rights in, or the right to encumber, the fixtures and personal property; and that at the time of filing the security interest will have attached under RA9.²³³

c) Priority

Except in very rare instances involving complex, Article 9 secured, large dollar transactions with specialized and valuable collateral, an opinion on priority of a security interest is not appropriate.²³⁴ This principle remains true more than ever under RA9 because (1) its mandatory choice of law rules frequently may involve more than one jurisdiction, and under the “debtor’s location governs perfection” rules that may not be the jurisdiction of the opinion giver; (2) detailed internal priority rules exist throughout the UCC, not just in RA9; (3) there are other state and federal statutory lien and

232. See *supra* notes 216–17 and accompanying text.

233. One or more of these assumptions may be stated elsewhere in the opinion, in the discretion of the opining lawyer, and as may be acceptable to the recipient. It is also understood that such opinions do not specifically address the issues of attachment, perfection, or priority, and do not rise to the level of a “full-bore” Article 9 opinion.

234. This should be true even if one or more perfection opinions are requested, and the opining lawyer has considerable substantive expertise in, and experience with, *Revised Article 9*. See GLAZER, *supra* note 140, § 12.8, at 431–32; 2003 *TriBar RA9 Report*, *supra* note 1, at 1454, 1460, 1477–78.

specialized laws (such as bankruptcy and “hot goods” laws)²³⁵ that can prime RA9 security interests; (4) the difficulty posed by searching for conflicting security interests, particularly given the recent transition to RA9 in over fifty jurisdictions; and (5) it is virtually impossible to determine with absolute certainty the ownership status of personal property.²³⁶

As a result, it is recommended that all opinions expressly state that the opining lawyer is not giving an opinion on perfection or priority unless it has been expressly agreed that such an opinion be given.

We express no opinion as to matters of title, priority, or perfection of liens or priority or perfection of security interests, except as set forth specifically herein.

iii) Multi-State Transactions

If the collateral is of a type for which perfection is by filing, RA9 requires the filing for personal property to be in the state in which the debtor is located (for corporations, limited liability companies, and limited partnerships, the state in which the entity is formed). This may be a different state from that where the debtor does business and where the personal property is located. As a result, Arizona counsel may be asked to give an opinion relating to a client that was formed under the laws of another state, or Arizona counsel may be asked to give an opinion as local counsel about perfection for an Arizona entity when counsel in another state is giving the general enforceability opinion about the transaction. In either event, if fixtures are involved, such perfection will be governed by the version of RA9 effective in the state in which the fixtures are located, which usually will involve recording the security agreement (which may be a deed of trust or mortgage) or recording a fixture filing financing statement, or both) in the county where the real property is located.

a) Debtor “Located” Outside Arizona

If the debtor is an entity formed outside Arizona, but the Arizona opining lawyer will give the enforceability opinion about the transaction, then the lawyer needs to work out as early as possible with the recipient and its

235. *See, e.g.*, *Citicorp Indus. Credit, Inc. v. Brock*, 483 U.S. 27, 39 (1987) (holding that the Federal Fair Labor Standards Act is applicable to secured creditors who acquire “hot goods” pursuant to a security agreement).

236. The recent introduction of security interest insurance policies, such as the First American “Eagle 9” Policy, provide recipients and lenders with an opinion alternative analogous to title insurance, thereby lessening any perceived need to address perfection or priority or both in third-party legal opinions.

counsel just how any requested perfection opinions will be addressed. There are at least four possible responses, some of which are interrelated.

First, an Arizona opining lawyer may decline to provide any opinion as to perfection by filing in any jurisdiction outside of Arizona, limiting any perfection opinion to any fixture filing because of the location in Arizona of particular fixture collateral. This approach may be coupled with a second but related response, which is to have any out-of-state perfection by filing addressed by counsel in such state. This may not turn out to cause any significant added burden and expense if counsel in that state already has been or must be employed to address issues of formation, organization, and good standing of one or more debtor entities. If the personal property collateral to be perfected by such an out-of-state filing is minimal or insignificant in value to the transaction viewed as a whole, then the recipient should be willing to consider whether it is really necessary at all.

A third response would be for the Arizona opining lawyer to assume that the filing laws of the other state are identical to those of Arizona (which may be a reasonable assumption under RA9), that the debtor organization is indeed located in that state, that the other state's filing office is the correct office at which to file, and that the form of financing statement is the proper form to use in that state, and therefore, based on those assumptions, to address perfection by filing as though Arizona law did so apply. This alternative involves making several intellectually questionable assumptions but may provide the recipient with a sufficient, albeit minimal, level of comfort regarding central filing.

The fourth response would be to address perfection in a manner that is expressly limited to and based upon a review of the UCC perfection and filing laws of the out-of-state jurisdiction only, and concluding that while an opinion is not being rendered, the opining lawyer believes that the central financing statement is in proper form and that security interests in central-filing collateral would be perfected by filing at a designated office in the other state. A variation of this approach would be to go ahead and render what is an opinion based on non-Arizona law as to this limited issue. This last variation could be appropriate if the opining lawyer already is willing and able to provide a formation and existence opinion as to Delaware or Nevada entities that are debtors for purposes of perfection by filing as to particular collateral or classes of collateral.

Given the recent effectiveness of RA9 nationally, it is likely that customary practice in rendering opinions as to UCC perfection will continue to evolve, and therefore cannot be considered settled or established at this time.

b) Debtor Located in Arizona – Local Counsel Opinion

If other counsel is giving the enforceability opinion, the form of opinion for an Arizona registered organization set forth above under perfection will be appropriate for the opining Arizona local counsel to give, with limitations and qualifications appropriate for local counsel opinions.

iv) Other Issues

This Report does not address issues of automatic perfection (sale of promissory notes and payment intangibles), perfection by possession (goods, instruments, tangible chattel paper, money, negotiable documents, and certificated securities), or perfection by control (investment property, letter-of-credit rights, deposit accounts, and electronic chattel paper), nor the full range of issues involved in rendering “U.C.C. security interest opinions.”²³⁷

While not exhaustive, a general methodology for any opining lawyer faced with those or any other issues under RA9 would be: determine applicable law as to each issue to be addressed; determine location and exact correct legal name of debtor(s); determine characterization of collateral and its consequences as to applicable law, mode(s) of perfection or any other special treatment under RA9 or the UCC (especially Article 8 as to “investment property”); attempt to limit collateral to that perfected only by filing; determine whether there are security interest(s) being granted in authenticated security agreements, and whether financing statements are in proper form and adequately completed (required information and not subject to rejection upon filing); determine place(s) for perfection to occur; determine if any aspect of the transaction is a sale rather than an encumbrance; make necessary assumptions or establish appropriate qualifications or exclusions; and try to limit the scope of any opinions with the recipient and its counsel to what is involved and truly important in the particular transaction in question, weighing cost, benefit, and risk to all concerned (former Article 9 checklists should not determine and dictate RA9 customary practice).

f. Special Issues – Real Estate Liens

An enforceability or remedies opinion includes within its scope an opinion about the validity of any real estate consensual real property liens created in the transaction. Absent any express exclusions or limitations, this

237. For a discussion of these topics, see, for example, GLAZER, *supra* note 140, §§ 12.1–12.11; 2003 *TriBar RA9 Report*, *supra* note 1, at 1457–1519.

opinion should be understood to include that the document contains the required operative content and terms to create such a lien,²³⁸ that there is an adequate legal description of the realty (and related interests) to be encumbered thereby,²³⁹ and that there is at least an explicit or implicit application of Arizona law to the creation and potential enforcement of the same. Absent any other express treatment, an enforceability or remedies opinion regarding such liens does *not include or address* issues of title or priority of lien, and the details of the mechanics of recordation will typically be assumed, at least in part, in the assumption portion of the opinion.

Title insurance validating the validity and priority of the mortgage lien is almost always obtained by the lender in connection with any transaction that includes real estate in its collateral. Both standard and extended coverage lender's policies insure that the lender's lien is valid and indicate relative priority with respect to other disclosed liens. Nevertheless, Arizona opining lawyers with some frequency are asked to render a specific opinion about the validity of consensual real estate liens.

The revised Illustrative Opinion provides the following example of an express opinion separately addressing a real estate-secured lien:

The deed of trust [mortgage] is sufficient in form to create a valid lien in favor of the Lender upon the Company's interest in the real property described therein and to be recorded in the real property records of the county recorder of the county in which the property is located [, and upon recordation will impart constructive notice of the lien to third parties].

i) General

In rendering either a general enforceability or a specific valid lien opinion, the opining lawyer should consider the following:

There must be an interest capable of being so encumbered. "Any interest in real property capable of being transferred may be mortgaged."²⁴⁰ Fee simple interests, leases, easements, beneficial and legal interests under agreements for sale, water rights, assignments of rents, and other interests in real property are capable of being encumbered. (There is some overlap here with RA9 security interests.)²⁴¹

238. See ARIZ. REV. STAT. ANN. §§ 33-402(4), 33-701 to -750, 33-801 to -821 (2000 & Supp. 2005) (discussing mortgages and deeds of trust, respectively).

239. This may be accomplished by an appropriate assumption.

240. ARIZ. REV. STAT. ANN. § 33-701(A) (2000); see also *id.* § 1-215(30), (33)–(34) (Supp. 2005) (defining real and personal property).

241. See *supra* Part II.B.8.e.

There must be a written instrument. “A mortgage may be created, renewed or extended only by [a] writing.”²⁴²

The writing must be subscribed (signed or authenticated, if a security interest is included) and acknowledged.²⁴³ The acknowledgment may be performed in or out of Arizona,²⁴⁴ but if undertaken outside Arizona, must comply either with Arizona law²⁴⁵ or with the laws of the place where the acknowledgement is taken.²⁴⁶ The words “subscribed and sworn to before me” may not comply with statutory requirements, or may constitute a jurat and not an acknowledgment, and should not be used standing alone without the addition of appropriate acknowledgment language.²⁴⁷ If the instrument is not acknowledged, it may be valid between the parties but upon recordation does not impart constructive notice to third parties.²⁴⁸

Although it is not clear under Arizona statutes whether delivery of a document is required, Arizona case law implies that delivery is necessary.²⁴⁹ Recording of a mortgage by the person who executed the instrument is prima facie evidence of delivery.²⁵⁰

An opining lawyer either should expressly assume the vesting of title in the mortgagor or beneficiary in the opinion or should rely by express reference on a title commitment or insurance policy as independently establishing the vesting of title.²⁵¹ “A mortgage gives the mortgagee no greater interest than the mortgagor possesses.”²⁵² A mortgage that purports to encumber property in which the mortgagor has no interest at the time the mortgage is executed is void; however, a mortgage may be given in anticipation of ownership.²⁵³

242. ARIZ. REV. STAT. ANN. § 33-701(B) (2000).

243. *See id.* §§ 33-401, 33-701, 47-9203(B)(3)(a) (2000 & Supp. 2005).

244. *See id.* § 33-501 (2000).

245. *See id.* §§ 33-503 to -506. A.R.S. section 33-504(3) provides a safe harbor.

246. *See id.* § 33-504(2).

247. *See id.* § 33-504(3).

248. *See id.* § 33-411(A); *see also* Reid v. Kleyensteuber, 60 P. 879, 879–80 (Ariz. 1900) (holding that only instruments that are acknowledged, proven, or certified in the manner provided by law shall, by being filed for record, impart notice to subsequent purchasers); Heller v. Levine, 437 P.2d 983, 986–87 (Ariz. Ct. App. 1968) (holding that the fact that a mortgage was not properly acknowledged does not invalidate it, but makes it a contract which may be specifically enforced between the parties).

249. *See Heller*, 437 P.2d at 986 (stating that the burden of showing an improper delivery rests on the defendant and that possession of the deed by the grantee is prima facie proof of delivery).

250. *Wixom v. Ingham*, 515 P.2d 606, 608 (Ariz. Ct. App. 1973).

251. *See infra* Part III.A.3.

252. *Moeur v. City of Tempe*, 412 P.2d 878, 881 (Ariz. Ct. App. 1966).

253. *Valley Chevrolet Co. v. O.S. Stapley Co.*, 72 P.2d 945, 949 (Ariz. 1937).

Arizona's so-called "Blind Trust Act" requires that certain persons receiving an interest in property in a representative capacity disclose the names and addresses of the beneficiaries, principals, or wards for whom they hold title, and the trust or other agreement under which they act.²⁵⁴ While no longer expressly applicable to trustees of deeds of trust, this law should be considered as bearing on the title held by mortgagors or trustors who are clearly holding that title in a representative capacity.²⁵⁵

If real property is held as community property or as a homestead, both the husband and wife must sign the document.²⁵⁶ The interest of a joint tenant, however, may be mortgaged without the consent or concurrence of the joint tenant(s), as may be co-tenancy interests.²⁵⁷

The writing should contain sufficient words of mortgage and a description of the property; with the minimum language: "For the consideration of _____, I hereby convey to _____ the following real property (describing it), to be void upon condition that I pay, etc."²⁵⁸ The description need not be precise.²⁵⁹

It is not necessary to record a mortgage in order to make it enforceable between the parties.²⁶⁰ But a valid lien opinion often pertains to the existence of constructive notice of the lien to third parties, as well as its validity between the parties to the instrument itself. This opinion may be rendered before or after recordation of the document, but the opining lawyer's diligence and the assumptions stated or implicit in the opinion will vary depending upon the time and circumstances of the delivery of the opinion.

The writing should be recorded in the county in which the real property is located,²⁶¹ contain a caption briefly describing the nature of the instrument and any basis for indexing categories when recorded,²⁶² be

254. See ARIZ. REV. STAT. ANN. § 33-404 (2000).

255. See *id.* § 33-404(A)-(G) (noting certain exemptions).

256. *Id.* §§ 33-452 to -453.

257. *In re Garcia*, 11 B.R. 10, 11 (Bankr. D. Ariz. 1981); *Cooley v. Veling*, 505 P.2d 1381, 1382 (Ariz. Ct. App. 1973).

258. ARIZ. REV. STAT. ANN. § 33-402.

259. See *Mounce v. Coleman*, 650 P.2d 1233, 1236 (Ariz. Ct. App. 1982).

260. *Valley Nat'l Bank of Ariz. v. Avco Dev. Co.*, 480 P.2d 671, 675-76 (Ariz. Ct. App. 1971).

261. ARIZ. REV. STAT. ANN. § 33-411(A).

262. *Id.* § 11-480 (Supp. 2005) (specifying "magic margin" requirements for recordable form of documents). *But see Watson Constr. Co. v. Amfac Mortgage Corp.*, 606 P.2d 421, 427 (Ariz. Ct. App. 1979) (holding that failure of a document to contain a proper descriptive caption does not render document void as against subsequent lienholders if the county recorder accepts the document for recording and properly indexes it).

legible,²⁶³ and contain original signatures.²⁶⁴

ii) Deed of Trust Liens

If the writing is intended as a deed of trust with a power of sale, and the opinion provided (implicit in enforceability) or required (explicit reference to trust deed issues) is that the deed of trust will create a valid deed of trust lien as opposed to a valid lien, additional issues should be considered. Although substantial compliance with the statutory requirements may be sufficient to create a valid lien (devolving to a realty mortgage that may only be foreclosed judicially), strict compliance with the statutory requirements is probably necessary to create a valid statutory deed of trust lien.²⁶⁵

A valid deed of trust lien requires a “Trust Deed” or “Deed of Trust,”²⁶⁶ containing the mailing address of each trustor, trustee, and beneficiary,²⁶⁷ and containing a statutorily sufficient legal description.²⁶⁸

There should be a conveyance of real property to a trustee²⁶⁹ who is qualified to be such a trustee of a trust deed.²⁷⁰

If a deed of trust fails to comply with all of the deed of trust requirements, it may nevertheless be enforced as a mortgage if it complies with the mortgage requirements, or may be treated as an equitable mortgage.²⁷¹

A deed of trust may cease to qualify as a valid power of sale trust deed in Arizona if it encumbers, in whole or in part, trust property in Arizona and in one or more other states.²⁷²

263. ARIZ. REV. STAT. ANN. § 11-480(A).

264. *Id.*

265. *See Patton v. First Fed. Sav. & Loan*, 578 P.2d 152, 155–56 (Ariz. 1978). *But see In re Bisbee*, 754 P.2d 1135, 1137 (Ariz. 1988).

266. *See* ARIZ. REV. STAT. ANN. § 33-801(5).

267. *Id.* § 33-802(B) (2000).

268. *Id.* § 33-802(A).

269. *Id.* § 33-801(10). *But see Bisbee*, 754 P.2d at 1137–39 (holding that subsequent appointment by a beneficiary of a qualified trustee may retain or restore a trust deed with “power of sale” status).

270. ARIZ. REV. STAT. ANN. § 33-803 (Supp. 2005).

271. *See Shelton v. Cunningham*, 508 P.2d 55, 58–59 (Ariz. 1973) (exploring whether an outright sale or mortgage was intended in applying the equitable mortgage doctrine); *Merryweather v. Pendleton*, 372 P.2d 335, 340–41 (Ariz. 1962) (stating six conditions that influence the determination of whether the doctrine of equitable mortgage should be applied); *Heller v. Levine*, 437 P.2d 983, 986–87 (Ariz. Ct. App. 1968) (holding that an improperly acknowledged mortgage was not invalidated as an equitable mortgage).

272. ARIZ. REV. STAT. ANN. § 33-801(8).

g. *Special Issues – Intellectual Property*

Special issues arise regarding the perfection of a security interest in intellectual property. Federal statutes and case law have created a distinction between the perfection of a security interest in federally-registered copyrights and perfection of interests in other intellectual property, such as patents and trademarks. If a debtor has extensive intellectual property, the Illustrative Opinion may require qualification regarding perfection of liens affecting such collateral. This area of the law is constantly changing. The case law in this area has evolved from bankruptcy court decisions to district court decisions, and is now reaching higher appellate courts. The discussion below represents the state of the law as of the time of the issuance of this Report.

i) Federally-Registered Copyrights

The Copyright Act²⁷³ provides that “[a]ny transfer of copyright ownership or other document pertaining to a copyright, may be recorded in the [United States] Copyright Office.”²⁷⁴ A “transfer” under the Copyright Act includes any mortgage or hypothecation of a copyright, whether “in whole or in part” and “by any means of conveyance or by operation of law.”²⁷⁵ The grant of a security interest has been held to be within the definition of transfer under the Copyright Act.²⁷⁶ Therefore, perfection of a security interest in a federally-registered copyright can only be effected by recording the security interest with the United States Copyright Office.

Because a recording is required with the United States Copyright Office, a question arises whether there should be a simultaneous filing of a financing statement under the UCC to perfect a security interest in a registered copyright, and, a fortiori, whether the UCC is preempted by the Copyright Act. The comprehensive filing system created by the Copyright Act and the unique federal interests that are implicated in copyrights support the conclusion that the Copyright Act preempts state adoption of the UCC regarding perfection of security interests in federally-registered copyrights.²⁷⁷ Thus, recording a “transfer” in the United States Copyright

273. 17 U.S.C. §§ 101 to 1332 (2000).

274. *Id.* § 205(a).

275. *Id.* §§ 101, 201(d).

276. *In re Peregrine Entm’t, Ltd.*, 116 B.R. 194, 198–99 (Bankr. C.D. Cal. 1990).

277. *Id.* at 199; *see also* ARIZ. REV. STAT. ANN. § 47-9311(A)(1) (2005) (providing that filing a financing statement is not otherwise effective to perfect a security interest when property is subject to a federal statute).

Office, rather than filing a financing statement, appears to be the sole method for perfecting a security interest in a copyright.²⁷⁸

As a result of this apparent nuance in intellectual property law, the language of the Illustrative Opinion may require qualification in the event the debtor has filed copyright registrations with the United States Copyright Office. The following language could be added to the Illustrative Opinion:

When forms of assignment are recorded in the United States Copyright Office, all action necessary to perfect such security interest in that portion of the Collateral that constitutes federally-registered copyrights in which a security interest may be perfected will have been taken.

ii) Unregistered Copyrights

In light of the broadened definition of intangible property under RA9, the *Peregrine* case appears to be limited in the case of unregistered copyrights.²⁷⁹ In September 2002, the Ninth Circuit held that the Copyright Act does not preempt state application of RA9 of the UCC as to unregistered copyrights.²⁸⁰ *World Auxiliary Power* held that a financing statement is sufficient to perfect a security interest in an unregistered copyright²⁸¹ and thereby rejected two earlier bankruptcy court decisions: *Zenith Productions, Ltd. v. AEG Acquisition Corp.*²⁸² and *In re Avalon Software*.²⁸³ Both earlier decisions held that a recording of a security interest with the United States Copyright Office was required.²⁸⁴ Although *World Auxiliary Power* may provide some comfort to practitioners, there are no decisions directly on point from other jurisdictions. Thus, cautious counsel to the secured party may require the debtor to first record the unregistered copyright with the United States Copyright Office, then record the assignment of the copyright with the United States Copyright Office, and also file a financing statement in the appropriate office.

278. *In re Peregrine Entm't, Ltd.*, 116 B.R. at 203; see Jeffrey W. Warren & Carrie Beth Baris, *Proper Perfection Procedures for Intellectual Property*, 21 AM. BANKR. INST. J. 18 (2002), available at WL 21-MAY AMBKRIJ 18 (discussing proper perfection procedures respecting copyrights).

279. See *In re Peregrine Entm't, Ltd.*, 116 B.R. at 201-03; see also *In re World Auxiliary Power Co.*, 303 F.3d 1120, 1130 (9th Cir. 2002).

280. *In re World Auxiliary Power Co.*, 303 F.3d at 1125-26.

281. *Id.* at 1130.

282. 161 B.R. 50 (B.A.P. 9th Cir. 1993).

283. 209 B.R. 517 (Bankr. D. Ariz. 1997).

284. *In re World Auxiliary Power Co.*, 303 F.3d at 1130.

iii) Patents and Trademarks

The law regarding perfection of security interests in other forms of intellectual property is also not completely settled. Several courts have held that the Patent Act and the Lanham Act *do not* mandate recording assignments of less than a full and complete transfer of ownership. The Ninth Circuit has specifically held that the filing of a financing statement is sufficient to perfect a security interest in patents.²⁸⁵ Other courts have reached a similar conclusion with regard to trademarks.²⁸⁶ Nonetheless, a cautious practitioner may file a Financing Statement *and* record an assignment of a federally-registered trademark or patent in the appropriate filing office.

iv) Conclusion

An opining lawyer may wish to add a further qualification to the Illustrative Opinion to address the general uncertainty of the law in this area. A sample addition to the Illustrative Opinion follows:

The provisions of the Security Agreement are effective to create a valid security interest in that portion of the Collateral consisting of federally-registered copyrights, common law copyrights, trademarks or service marks, or applications for any such marks, and patents, to the extent that: (a) the Borrower has rights in such Collateral, and (b) a security interest in such Collateral may be granted pursuant to Article 9 of the Arizona Uniform Commercial Code. Under current law, upon the filing of the UCC1 Financing Statement in the manner described above, it appears that all action necessary to perfect a security interest in such Collateral (with the exception of federally-registered copyrights) will have been taken. Regarding federally-registered copyrights, under current law, upon the recording of the transfer with the United States Copyright Office, it appears that all action necessary to perfect a security interest in federally-registered copyrights will have been taken. The federal statutes governing trademarks and patents do not set forth the procedure for perfection and priority of liens

285. *In re Cybernetic Servs. Inc.*, 239 B.R. 917, 923 (B.A.P. 9th Cir. 1999).

286. *See, e.g., In re Together Dev. Corp.*, 227 B.R. 439, 441–42 (Bankr. D. Mass. 1998) (finding that the filing of a financing statement is sufficient to perfect a security interest in a trademark); *In re Roman Cleanser Co.*, 43 B.R. 940, 944 (Bankr. E.D. Mich. 1984), *aff'd*, 802 F.2d 207 (6th Cir. 1986); *In re TR-3 Indus.*, 41 B.R. 128, 131 (Bankr. C.D. Cal. 1984); *see also* Thomas M. Ward, *The Perfection and Priority Rules for Security Interests in Copyrights, Patents, and Trademarks: The Current Structural Dissonance and Proposed Legislative Cures*, 53 ME. L. REV. 391, 400 (2001) (discussing the problems and issues related to the perfection of security interests in intellectual property).

encumbering trademarks and patents in the same detail as in the United States Copyright Act. Accordingly, certain courts have reached the conclusion that the Lanham Act and the Patent Act do not preempt state law and that recordation of a security interest with the United States Patent and Trademark Office is not required to perfect an otherwise valid security interest. *In re Cybernetic Services, Inc.*, 239 B.R. 917, 920 (B.A.P. 9th Cir. 1999); *In re Together Development Corp.*, 227 B.R. 439, 441 (Bankr. D. Mass. 1988); *In re TR-3 Industries*, 41 B.R. 128, 131 (Bankr. C.D. Cal. 1984). However, there is no guarantee that filing the Financing Statement in the manner described above alone will be sufficient in the future to maintain a perfected security interest in patents, federally-registered trademarks or service marks, or applications for such marks.

h. Bankruptcy Remote Entities

When originating real property secured commercial loans for sale into rated securitization transactions, lenders may require the Borrower to demonstrate that the Borrower is structured to make it less likely to become insolvent as a result of its own activities and is adequately insulated from the consequences of the insolvency of certain other parties. To accomplish these objectives, the encumbered property must be isolated from: (a) the equity holders and affiliates of the Borrower; (b) the poor performance of other properties which may be owned by the Borrower or its affiliates; and (c) any debts and obligations other than the loan and the ordinary trade debt of the Borrower related to the ownership and operation of the real property. In this context, the Borrower's counsel may be asked to provide what has come to be known as a substantive non-consolidation opinion, opining: (i) that the borrower is a "bankruptcy-remote," single- or special-purpose entity ("SPE"), which has no assets other than the encumbered property, conducts no business other than the operation of the mortgaged property, and has no debts beyond the loan and reasonable trade debt related to the mortgaged property; and (ii) that if an equity holder or affiliate entity or control person of the Borrower were to become a debtor in a bankruptcy proceeding, the court would not order substantive consolidation of the affiliate or equity holder with the Borrower.²⁸⁷

287. "Substantive consolidation is the merger of separate entities into one action so that the assets and liabilities of both parties may be aggregated in order to effect a more equitable distribution of property among creditors." *In re Baker & Getty Fin. Serv., Inc.*, 78 B.R. 139, 141 (Bankr. N.D. Ohio 1987).

Lenders typically attempt to ensure the isolation necessary to satisfy SPE status by requiring that the Borrower entity's organizational documents contain various limits and prohibitions on the Borrower's activities. For example, the Borrower's stated purpose is usually limited to owning and operating the encumbered property, and the Borrower's consolidation or merger with another entity, the sale of substantially all of its assets, the incurrence of additional debt, and the amendment of its organizational documents are all typically prohibited. In addition, the organizational documents typically are required to provide that: (a) the Borrower's indemnification of its directors and officers (or their equivalents, if the Borrower is a limited partnership or a limited liability company) are fully subordinated to the entity's obligations respecting the encumbered property; and (b) the entity must observe various other separateness covenants (e.g., to establish and maintain offices and entity records separate from any parent or affiliate, to refrain from commingling its assets with those of any affiliate, or from guaranteeing debts of any other entity, etc.) designed to underscore the Borrower's separateness from its parent, affiliates, and equity holders. There may also be limitations on dissolution and voting and an "independent director" may be required to represent the lender's interests on the corporate board. If the Borrower is a limited partnership or limited liability company, a second SPE (almost always a corporation) may need to be formed to act as the general partner or managing member, or as an outside member, and that such second SPE's organizational documents will need to contain analogous limitations and prohibitions as the Borrower's.

i) Substantive Consolidation

Historically, lenders were comforted by borrowers' diversification of assets and business operations, such diversification being perceived as strengthening a borrower's perceived ability to repay the loan. Today, however, because of the newly emerging doctrine of substantive consolidation, real property secured lenders generally operate under a different paradigm. Derived from the general equitable powers granted to bankruptcy courts by Section 105(a) of the Bankruptcy Code,²⁸⁸ substantive

288. The practice of substantive consolidation is not expressly authorized under the Bankruptcy Code. Bankruptcy Rule 1015 does provide for joint administration of cases; however, the Advisory Committee Notes thereunder state that "[c]onsolidation, as distinguished from joint administration, is neither authorized nor prohibited by this rule since the propriety of consolidation depends on substantive considerations and affects the substantive rights of the creditors of the different estates." FED. R. BANKR. 1015 cmt. b. Accordingly, the power to substantively consolidate derives from the general equity jurisdiction of a court of bankruptcy under Section 105(a) of the Bankruptcy Code. *In re Richton Int'l Corp.*, 12 B.R. 555, 557 (Bankr. S.D.N.Y. 1981).

consolidation provides that two or more entities which look and act like a single entity *prior to* bankruptcy also should be treated as a single debtor *in* bankruptcy. Thus, depending on how affiliated entities were operated before one of them files bankruptcy, a bankruptcy court may rely on this doctrine to reach the assets of a non-debtor entity which it deems sufficiently affiliated with the debtor entity.²⁸⁹

Courts have applied various factors on a case-by-case basis to determine whether substantive consolidation is appropriate. These include the following: (1) the degree of difficulty in segregating and ascertaining individual assets and liabilities; (2) the existence of consolidated financial statements; (3) the profitability of consolidation at a single physical location; (4) the commingling of assets and business functions; (5) the unity of interests and ownership between the various corporate entities; (6) the transfer of assets without formal observance of corporate formalities; (7) the treatment of the entities by creditors as a single economic unit, without relying on their separate credit when giving loans; (8) the existence of common officers and directors; (9) whether the parent company finances the subsidiary; (10) whether the parent company owns all or a majority of the capital stock of the subsidiary; (11) whether the parent incorporated the subsidiary; (12) whether the subsidiary is grossly undercapitalized; (13) whether the parent pays salaries, expenses, or losses of the subsidiary; (14) whether the subsidiary has substantially no business except with the parent; (15) whether the parent refers to the subsidiary as such or as a department or division of the parent; (16) whether the directors or officers of the subsidiary take directions from the parent; and (17) whether the subsidiary does not observe all corporate formalities.²⁹⁰

289. There is limited case law specifically addressing the legality of substantive consolidation of a debtor and a nondebtor affiliate, and a split of authority exists. The majority rule is that creditors not having claims against nondebtor affiliates may implead parties alleged to be the “alter ego” of the debtor. *E.g., In re Crabtree*, 39 B.R. 718, 722–26 (Bankr. E.D. Tenn. 1984). Other cases, however, refuse to recognize any jurisdiction over nondebtor affiliates and/or shareholders. *See, e.g., In re The Julien Company*, 120 B.R. 930, 938 (Bankr. W.D. Tenn. 1990) (finding that motion to consolidate debtor corporation with nondebtor shareholder violates due process rights of nondebtor and its separate creditors). In the only decision by the United States Supreme Court on this issue to date, *Sampsel v. Imperial Paper & Color Corp.*, 313 U.S. 215 (1941), the Court held that substantive consolidation of a nondebtor corporation into an individual debtor’s estate was proper where the transfer of property by the individual to the corporation was not in good faith and was made for the purpose of placing it beyond the reach of the individual’s creditors, and where the effect of the transfers was to hinder, delay, or defraud the individual’s creditors—so ruling despite the Court of Appeals’ holding that the nondebtor corporation could not be deemed the alter ego of the individual debtor under applicable state law.

290. *See generally In re Gulfco Inv. Corp.*, 593 F.2d 921 (10th Cir. 1979); *Soviero v. Franklin Nat’l Bank of Long Island*, 328 F.2d 446 (2d Cir. 1964); *In re Stop & Go of Am., Inc.*,

While the risk of substantive consolidation is substantially diminished through the Borrower's organization as an SPE, and through its observance of the above-listed "separateness covenants" set forth in its organizational documents and in the loan documents, there can be no guaranties about the conclusions of courts in general, and bankruptcy courts in particular, on these issues.²⁹¹

ii) When Non-Consolidation Opinions Are Required

Typically, non-consolidation opinions are required when an SPE Borrower is controlled by a non-SPE affiliate. Control, for this purpose, is determined by the non-SPE affiliate's ability to cause the SPE Borrower to breach its separateness covenants and thereby subject itself to substantive consolidation. An equity holder possessing more than a 49% interest in the borrower is generally deemed to control the Borrower, and, if that equity holder is a non-SPE, an opinion may be required to analyze the Borrower's relationship with that controlling equity holder. Note, however, that in any situation there will be some person or entity in a position to cause the Borrower to breach; the Committee cautions against the opining lawyer assuming that risk.

Additionally, a non-consolidation opinion may also be required to analyze the relationship between an SPE Borrower and any individual or

49 B.R. 743, 747 (Bankr. D. Mass. 1985); *In re Tureaud*, 45 B.R. 658 (Bankr. N.D. Okla. 1985). The courts recognize that these factors should not be mechanically applied and are not dispositive, but that they must be evaluated in the overall "balancing of equities" for and against consolidation. *In re Donut Queen, Ltd.*, 41 B.R. 706, 709 (Bankr. E.D.N.Y. 1984) (holding that the party proposing consolidation bears the burden of demonstrating that prejudice resulting therefrom is outweighed by the benefit to be obtained).

291. Some courts recognize that as a general rule "[t]he power to consolidate should be used sparingly because of the possibility of unfair treatment of creditors of a corporate debtor who have dealt solely with that debtor without knowledge of its interrelationship with others." *Chem. Bank N.Y. Trust Co. v. Kheel*, 369 F.2d 845, 847 (2d Cir. 1966). Other courts have adopted a more "modern" or "liberal" trend toward allowing substantive consolidation, on the theory that the doctrine "has its genesis in the increased judicial recognition of the widespread use of interrelated corporate structures by subsidiary corporations operating under a parent entity's corporate umbrella for tax and business purposes." *Eastgroup Properties v. S. Motel Ass'n, Ltd.*, 935 F.2d 245, 248-49 (11th Cir. 1991). The Ninth Circuit has recently taken a balanced approach, holding that a sufficient basis for consolidation exists when either of two factors are present: "(1) whether creditors dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit; or (2) whether the affairs of the debtor are so entangled that consolidation will benefit all creditors." *In re Bonham*, 229 F.3d 750, 766 (9th Cir. 2000) (citing *In re Reider*, 31 F.3d 1102, 1108 (11th Cir. 1994)). While the enunciated factors seem to be consistently applied for the most part, cases are to a great degree *sui generis* and precedents are of limited value. See *In re Reider*, 31 F.3d 1102, 1108 (11th Cir. 1994); see also LEGAL OPINION LETTERS, *supra* note 145, at 10-20 (discussing these issues more fully).

entity that may affect the SPE Borrower's ability to pay the loan or the status of the encumbered property. For example, a non-consolidation opinion may be required to analyze the SPE Borrower's relationship with a property manager that exercises control over the encumbered property.

iii) Drafting the Opinion

In deciding whether or not to consolidate SPE Borrowers with affiliates, bankruptcy courts conduct facts-and-circumstances analyses for each case; obviously, as a practical matter, an attorney cannot authoritatively opine as to what a court will do.²⁹² A non-consolidation opinion, therefore, must be a reasoned opinion, containing a complete statement of the facts relied upon and a full discussion of the legal analysis used to reach the conclusion. Because of this uncertainty, the lender must be comfortable with the attorney's thorough understanding of the law in this area, and this understanding must be demonstrated in the opinion.

Parties to Whom the Opinion is Addressed: The opinion should be addressed to the lender, to the extent known, to the agencies that will be rating the pool in which the loan will be included, and to the trustee for the securitization transaction. To the extent that the names of these persons are not known, the opinion may state that it may be relied upon by:

any rating agency rating the debt,

and by:

any trustee of a trust formed in connection with the securitization transaction into which the loan is conveyed.

Parties Subject to the Opinion's Analysis: The opinion should clearly state which relationships its analysis addresses, and which relationships the attorney was requested to analyze. The following language is illustrative:

We have been asked to render our opinion as to whether, in the event that [non-SPE Affiliate] (the "Affiliate") were to become a debtor in a case under Title 11 of the United States Code (the "Bankruptcy Code"), a court of competent jurisdiction, exercising reasonable judgment after full consideration of all relevant factors, in a properly presented and argued case, would recognize the separate existence of the Borrower, on the one hand, and the Affiliate, on the other hand, and accordingly, would not order the substantive consolidation of the assets and liabilities of the Borrower with those of the Affiliate.

292. See *supra* notes 288–89.

Documents Reviewed: Because non-consolidation opinions are so fact-intensive, the opining lawyer must demonstrate a thorough knowledge of the structure of the transaction. Therefore, the opinion should state that the opining lawyer has reviewed every document in the transaction, and each of those documents should be specifically listed.

Factual Assumptions: The opinion should describe all the relevant facts considered by the opining lawyer. It is the core function of the opinion to develop the facts of a transaction, because an accurate and complete recitation of the facts gives credibility to the opinion and can lead a sophisticated recipient to independently reach the conclusion that the Borrower (or other relevant party) will not be subject to substantive consolidation. The factual assumptions may be categorized as “Loan Structure Assumptions,” which describe the entities covered by the opinion and their relationships to each other and to the encumbered property, and “Separateness Organizational Assumptions,” which tie together applicable separateness factors with the Borrower’s contractual commitments and organizational structure. The Committee recommends that the opining lawyer expressly assume that the Borrower is not insolvent or subject to bankruptcy proceedings at the date of the opinion, will not be rendered insolvent by the contemplated transactions, will comply with all laws, will observe all corporate formalities without limitation, and will comply with all of its obligations under the loan documents.

Legal Analysis: The opinion should describe: (i) the nature and evolution of the substantive consolidation doctrine, with all major tests upon which reliance is placed by courts, and (ii) how a court would apply those tests to the facts of the Borrower’s transaction. Both the favorable and the unfavorable facts should be discussed to assure the recipient that the opining lawyer has contemplated all aspects of the legal analysis and to demonstrate a full understanding of the law.

Conclusion: The opinion should conclude that a court would not order substantive consolidation of the Borrower with any of the described affiliates based on the facts surrounding the loan transaction. The following language is illustrative of a concluding statement:

Based on the foregoing, and subject to the assumptions, qualifications, and discussions contained herein and the reasoned analysis of analogous case law, it is our opinion that, in the event that [Non-SPE Affiliate] were to become a debtor in a case under the Bankruptcy Code, in a properly presented and argued case, a court of competent jurisdiction would recognize the separate existence of borrower and [Non-SPE Affiliate], and, accordingly,

would not order the substantive consolidation of the assets and liabilities of borrower and [Non-SPE Affiliate].

Qualifications: It is generally acceptable to qualify the foregoing opinion with a statement underscoring the inherent uncertainty in this area. For example:

Although the foregoing opinion is based upon an analysis of the assumed facts in light of current applicable law, all as set forth above, we can give no assurance that a creditor or trustee of [the SPE] in a federal bankruptcy proceeding would not attempt to have the assets and liabilities of [the SPE] substantively consolidated with those of an equity holder or Affiliate. Further, we express no opinion with respect to the availability of a preliminary injunction or other temporary relief pursuant to broad equitable powers granted to a federal bankruptcy court pending a final determination on the merits.

We advise you that there are a number of inherent limitations in an opinion of this nature, including the pervasive equitable powers and discretionary judgment of the bankruptcy judge reviewing the facts and circumstances as they may exist at a future time; the overriding congressional goal of promoting reorganizations to which other legal rights and policies may be subordinated; the interplay of facts, circumstances, relationships and other considerations, some of which may not now exist; and the inherently equitable nature of the bankruptcy process. Further, an opinion is not a guaranty of what a court would hold, rather an informed judgment as to a specific question of law. Thus, this opinion is not a prediction of what a court would actually hold, but an opinion as to the decision a court would reach if the issue were properly presented to it and the court followed existing legal precedents applicable to the subject matter of this opinion.

It is also appropriate, if necessary, for the opining lawyer to express reliance on the certificates of the Borrower and/or of one or more directors, officers, or other “control persons” of the Borrower, with respect to factual statements made in the opinion, and the Borrower’s or other person’s (as applicable) intent to perform the separateness covenants and other obligations described in the opinion.

iv) Assumption and Modification Transaction

A lawyer may be asked to render an enforceability opinion concerning a modification or assumption of existing transaction documents. The modification or assumption documents will often contain covenants

purporting to ratify or incorporate by reference the terms of the existing transaction documents. As a result, an enforceability opinion rendered in connection with the assumption or modification documents would be deemed to extend to the enforceability of the existing transaction documents.

In most cases, the same or another lawyer may have already rendered an opinion concerning the enforceability of the existing transaction documents. In those instances, it may be appropriate for the opining lawyer to assume that the existing transaction documents are enforceable in accordance with their terms. When such an assumption is made, the effect of the opining lawyer's enforceability opinion as to the modification or assumption documents is limited to the enforceability of the modification or assumption itself, as opposed to the enforceability of the existing transaction documents. The following assumption is provided as an illustration:

We have assumed that the Existing Documents²⁹³ are valid, binding, and enforceable obligations of the parties thereto, enforceable against the parties thereto in accordance with their respective terms.

C. Knowledge and Materiality Limitations

In the Illustrative Opinion, the opining lawyer's opinion regarding certain factual matters is qualified by the statement "we have no knowledge" or "to our knowledge."²⁹⁴ This qualification indicates that the opinion is not to be read literally, but in the context of customary practice.²⁹⁵ No single broad definition of knowledge has gained general acceptance, nor does a knowledge qualification lessen the opining lawyer's customary diligence necessary to support the opinion.²⁹⁶ In the context of this Report, the term "knowledge," unless otherwise defined, is limited to actual knowledge—the current "conscious awareness," of the lawyer or group of lawyers preparing the opinion.²⁹⁷ This definition recognizes that what might

293. The opining lawyer should define "Existing Documents" by listing the documents that are included in the definition.

294. Other common qualifications include "to the best of our knowledge," "we do not know of," "known to us," "to our knowledge after due inquiry," and "to our knowledge after appropriate diligence." Certain lawyers believe there is no significant difference among these phrases. See 1998 *TriBar Report*, *supra* note 1, § 2.6.1, at 618–19.

295. Use of the term "knowledge," however, does not negate a lawyer's ethical obligations. See *infra* Section III.A.

296. See 1998 *TriBar Report*, *supra* note 1, § 2.6.1, at 618–19.

297. 1991 *Accord*, *supra* note 3, § 6.A, at 190.

have been known at one time may have been forgotten.²⁹⁸ The opining lawyer is under no obligation to consult with all members of the firm or peruse the entirety of the firm's files to confirm the accuracy of any factual matter or validity of any underlying assumption.²⁹⁹ Because such an investigation could entail substantial delay and expense with, potentially, a disproportionately small probability that anything of value would be discovered, it is sufficient for the opining lawyer to consult with other members of the firm actively participating in negotiating the transaction, preparing the transaction documents, or preparing the opinion.

There are circumstances, however, where an opinion recipient may desire that an opining lawyer inquire of other lawyers in the firm or consult additional firm files. For example, another lawyer not actively participating in the preparation of the opinion may represent the client in other matters and thus possess relevant information. Similarly, an opinion recipient might have some reason to suspect that there is relevant information in unrelated case files that is not within the conscious awareness of the lawyers actively preparing the opinion. In these circumstances, an opinion recipient might request that the definition of knowledge be expanded to include the consultation with, or review of, other firm lawyers or files.

The recipient of an opinion should not assume that the opining lawyer has made any investigation beyond that required by the above definition of knowledge. Where specific investigation is requested of the opining lawyer, the opinion should state the scope of the investigation actually undertaken. Conversely, when the opining lawyer has not exercised customary diligence, the opinion should make clear the limited investigation undertaken and that no other investigation was conducted. This can be accomplished by adding the phrase, "without investigation."³⁰⁰

The qualifying term "material" is sometimes used in opinions. Although the opining lawyer may believe that the use of said term may act to limit the scope of disclosure, its use places on the opining lawyer the burden of making judgments about, for example, the potential magnitude of adverse litigation and its potential impact on the client's financial condition or operations. This burden may be reduced by adopting a definition of material that excludes items that do not exceed a specified dollar amount.³⁰¹ The opining lawyer, however, may still be burdened with difficult decisions

298. *See id.*

299. 1998 *TriBar Report*, *supra* note 1, § 2.2.2, at 613–15; *Legal Opinion Principles*, *supra* note 1, § III.B., at 833.

300. 1998 *TriBar Report*, *supra* note 1, § 2.6.1, at 619.

301. *See* ACREL/ABA *Guidelines*, *supra* note 140, § 3.2, at 248.

about whether pending litigation involving claims for non-monetary damages qualifies as material.

D. Assumptions

The opinions set forth in an opinion are subject to commonly recognized assumptions. Certain assumptions should be set forth explicitly in the body of the opinion. Others are generally thought to be so basic to the opinion process that they need not, but may be, explicitly stated. In either case, an opining lawyer may not make an assumption contrary to the opining lawyer's knowledge, unless the assumption and the opining lawyer's contrary knowledge are expressly stated in the opinion, and the party receiving the opinion either consents to or requests the assumption.³⁰²

The assumptions portion of the opinion may well contain the following introductory paragraph:

With your permission, in rendering the foregoing opinions, we have made the following assumptions. We have made these assumptions without independent verification, and with the understanding that we are under no duty to inquire or investigate regarding such matters; [however, we have no knowledge of any facts that we know to be inaccurate or any factual representations that we know to have been provided under circumstances making reliance unwarranted.]³⁰³

1. Stated Assumptions

The Committee recommends that the following assumptions, if applicable in a particular transaction, be expressly stated:³⁰⁴

(1) The genuineness of all signatures not witnessed (or, that each document will be or has been executed by the persons designated on the document to sign). In many cases, the party requesting the opinion will require that this assumption be limited to the genuineness of signatures of persons other than the opining lawyer's clients. If the opining lawyer does so limit this assumption, the opining lawyer must be sure that the clients'

302. See also *infra* Section III.C.

303. But see *infra* Section IV.B.2.c. (discussing the obligation of the opinion lawyer to disclose inaccurate or unwarranted assumptions).

304. This list of stated and implicit assumptions includes the assumptions listed in the 1991 *Accord*, *supra* note 3, although many of these have been rewritten in light of the Committee's experience with current practice. Several additional assumptions also are listed, again in accordance with perceived current practice.

signatures are indeed genuine, either by actually witnessing the signatures or taking other measures to assure genuineness. This may be a problem with respect to signatures of spouses or minority owners who have not been active in the entity or with respect to parties who are in remote locations.

(2) That each client who is a natural person, and who is executing any of the documents or otherwise involved in the transaction, possesses the legal competency and capacity necessary for such individual to execute such documents and/or to carry out such individual's role in the transaction.

(3) That the documents accurately and completely describe and contain the parties' mutual intent, understanding, and business purposes, and that there are no oral or written statements, agreements, understandings, or negotiations, nor any usage of trade or course of prior dealing among the parties, that directly or indirectly modify, define, amend, supplement, or vary, or purport to modify, define, amend, supplement, or vary, any of the terms of the documents or any of the parties' rights or obligations thereunder, by waiver or otherwise.³⁰⁵

(4) That the applicable documents, immediately after delivery, will be properly filed or recorded in the appropriate governmental offices,³⁰⁶ that the recipient will timely file all necessary continuation statements, and that all fees, charges, and taxes due and owing as of this date have been paid. [For use where the opining lawyer is not responsible for recordation or filing.]³⁰⁷

(5) That the result of the application of Arizona law as specified in the documents will not be contrary to a fundamental policy of the law of any other state with which the parties may have contact in connection with the documents. [For use in an enforceability opinion, where the documents choose Arizona choice of law, and if choice of law is not expressly excluded from the opinion.]

(6) That the recipient will receive no interest, charges, fees, or other benefits or compensation in the nature of interest in connection with the transaction other than those that the Client (and, where applicable, the Guarantor) has agreed in writing in the documents to pay. [For use in a loan transaction, in light of the language of A.R.S. Sections 44-1201, 44-1202.]

305. See generally *Darner Motors Sales, Inc. v. Universal Underwriters Ins. Co.*, 682 P.2d 388 (Ariz. 1984).

306. In certain cases, the opining lawyer may be asked to opine what the appropriate governmental offices are and in that case it should be the subject of a separate opinion.

307. This assumes that the documents have not been prefiled.

(7) Where tangible personal property (personalty) is to be acquired after the date hereof, that a security interest is created under the after-acquired property clause of the Security Agreement. [For use in a personal property secured loan transaction.]

(8) Our opinions as to personalty and fixtures cover only (i) security interests created under Chapter 9 (RA9) of the Arizona UCC, (ii) only UCC collateral or transactions, and (iii) UCC perfection methods [limited to filing financing statements].

(9) That the note will be duly delivered for value and for the consideration provided for in, or contemplated by, the documents and that value has been given for the creation of any security interest.

(10) That the client (and, where applicable, the guarantor) holds the requisite title and rights to any real property or personalty involved in the transaction or otherwise purported to be owned by it.

2. Implicit Assumptions

The Committee believes that the following assumptions are, under current practice, generally thought to be so basic to the opinion process that they are understood to be applicable to all Arizona opinions, even if not expressly stated. However, it is common practice for opining lawyers to include some or all of the following assumptions in their opinions, although including any one of the following will not necessitate the inclusion of the others:

(1) That all statutes, judicial and administrative decisions, and rules and regulations of governmental agencies, constituting the law of the relevant jurisdiction, are generally available (i.e., in terms of access and distribution following publication or other release) to lawyers practicing in the jurisdiction, and are in a format that makes legal research reasonably feasible.³⁰⁸

(2) That the constitutionality or validity of a relevant statute, rule, regulation, or agency action is not in issue unless a reported decision of an appellate court in the relevant jurisdiction has

308. Practitioners may deal with Native American law; these organic sources of law may not be as clear as Arizona law. Consequently, the opining lawyer may consider adding the following assumption to clarify where the relevant law would be found:

That all relevant law of _____ is embodied in legislative actions, resolutions, judicial and administrative decisions, and rules and regulations of governmental agencies.

specifically addressed, but not resolved, or has established, unconstitutionality or invalidity.

(3) That all contracts to which the client is a party, or by which it or its property is bound, other than those evidenced by the documents, would be enforced as written.

(4) That all court and administrative orders, writs, judgments, and decrees that name the client and are specifically directed to it or its property would be enforced as written.

(5) That all certificates or other documents issued by any public official are complete and accurate.

(6) That all public records reviewed (including proper indexing and filing) are accurate, complete, and authentic.

(7) That all documents submitted as originals are authentic, and the conformity of each document that is a copy to an authentic original.

(8) That the description of the real and personal property contained in the deed of trust and the description of the personal property contained in the financing statement are legally sufficient to enable a subsequent purchaser or mortgagee to identify such property. [For use in a secured loan transaction.]

(9) That the documents and the transaction have been, to the extent necessary, duly and validly authorized, executed, acknowledged, and delivered by all parties other than the opining lawyer's client, and that all other legal requirements applicable to all other parties³⁰⁹ have been satisfied to the extent necessary to make the documents enforceable against all other parties in accordance with their terms.

(10) That all parties other than the opining lawyer's client have complied with all legal requirements pertaining to its status, as such status relates to its rights to enforce the documents against the Client.³¹⁰

(11) That such personalty constituting fixtures were and continue to be located on the real property collateral described in the Deed of Trust. [For use in a secured loan transaction.]

309. "All other parties" means parties other than the borrower and guarantor (i.e., the client of the opining lawyer).

310. The Committee interprets this assumption as focusing on the recipient's standing to enforce the documents against the client, as distinguished from the immediately previous assumption, which focuses on satisfaction of all conditions precedent to enforceability of the documents against the recipient.

(12) That the representations, warranties, and covenants in the documents and in the Officer's Certificates as they relate to factual matters relevant to our opinion are accurate.

(13) That none of the information, whether written or oral, that may have been made by or on behalf of the parties to the documents or otherwise contains any untrue statement of a material fact or omits to state a material fact necessary to make the statements made, in light of the circumstances in which they are made, not misleading.³¹¹

(14) That none of the other parties nor any of their lawyers have any current actual knowledge that any portion of the opinion is not accurate.

(15) That no person upon whom reliance is placed for purposes of this opinion has perpetrated a fraud upon any party to the documents, or upon the opining lawyer.

(16) That there has been no mutual mistake of fact or misunderstanding, duress, or undue influence. [May be qualified in certain securities opinions.]

(17) That the conduct of the parties to the transaction evidenced by the documents has complied with any requirement of good faith, fair dealing, or conscionability.

(18) That all parties other than the opining lawyer's client have acted without notice of any defense against the enforcement of any rights created by, or adverse claim to any property or security interest transferred or created pursuant to, the documents.

(19) That the client, subsequent to the date of the opinion, will obtain all permits and governmental approvals required in the future, and take all actions similarly required, relevant to the transaction evidenced by the documents or performance of the documents.

(20) That all parties to the documents and their successors and assigns will act in accordance with, and will refrain from taking any action that is forbidden by, the terms and conditions of the documents.

311. Whether or not the documents contain such covenants, there is debate about whether an opinion about enforceability of the modification or assumption documents also covers the existing transaction documents. The Committee recommends that the opinion specifically state either that the opinion covers the existing transaction documents or that it does not constitute an opinion about the existing transaction documents.

(21) That the parties to the documents and their successors and/or assigns will comply with all requirements of applicable procedural and substantive law in exercising any rights or enforcing any remedies under the documents.

(22) That the exercise of any rights or enforcement of any remedies under the documents would not be unconscionable, result in a breach of the peace, or otherwise be contrary to public policy.

(23) That the client will not in the future take any discretionary action permitted under the documents (including a decision not to act) that would result in a violation of law or constitute a breach or default under any other contract to which the client is a party or by which it or its property is bound, or under any court or administrative order, writ, judgment, or decree that names the client and is specifically directed to it or its property.

E. Use and Disclosure of and Reliance Upon Opinion by Addressee and Others

Ordinarily, only the recipient is entitled to rely on an opinion or assert any legal rights based on an opinion. Frequently, however, a client will request that the opining lawyer address the opinion to other third parties.³¹² If the opining lawyer intends that another third party rely on an opinion, the opinion or a separate writing signed by the opining lawyer should specify the identity of any third party intended to rely on the opinion, possibly by adding that third party to the list of addressees of the opinion.

Ordinarily, the recipient may not rely on an opinion for any purpose other than the purpose contemplated by the transaction documents. If the opining lawyer intends that the recipient rely on an opinion for any other purpose than the purpose contemplated by the transaction documents, the opinion or a separate writing signed by the opining lawyer should specify under what circumstances and to what extent the recipient may rely on the opinion. The Illustrative Opinion provides:

This opinion is being furnished to you solely for your benefit and may be relied on by you only for the purpose contemplated in the Transaction. Accordingly, it may not be: (i) used or relied upon by, or quoted to or delivered to, any other person or entity, or (ii) used or relied upon for any purpose other than the purpose

312. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 50-1, 91 (2000) (discussing the related issues of a lawyer's duty of care to clients and non-clients, and waiver of work product immunity).

contemplated in the Transaction without, in each instance, our prior written consent.

F. No Duty to Update

An opinion normally is dated the date of delivery, and speaks only as of that date, although it may deal in part with the availability of remedies in the future. An opining lawyer is not expected: (a) to update an opinion because of changes in the law or facts, or (b) to advise the recipient (or any third party) of changes in law or fact, unless the opining lawyer has expressly undertaken to do so. Although it is not necessary to state the absence of the duty, some opining lawyers do so in language similar to that contained in the Illustrative Opinion:

The opinions expressed in this letter are based upon the law and facts in effect on the date hereof, and we assume no obligation to update, revise, or supplement this opinion.

III. INAPPROPRIATE SUBJECTS FOR OPINIONS

Factual matters or matters involving intertwined fact and law issues, recognized legal uncertainties, and the laws of jurisdictions in which the opining lawyer is not licensed to practice are generally inappropriate subjects for opinions unless the lawyer possesses the necessary knowledge and experience to render the opinion. The “golden rule” is applicable in this context: A lawyer should not ask another lawyer to give an opinion that the requesting lawyer would be unwilling to give.

A. Factual Matters/Mixed Fact and Law Issues

A lawyer should neither give nor request opinions about factual matters beyond the scope of the lawyer’s legal expertise. An opinion should address matters of law, not merely confirm facts that the parties or other experts are better able to verify. For example, a lawyer should not render an opinion that a real property development project has an assured water supply for the next one hundred years, that the company has filed all necessary federal, state, and local tax returns, that legal title to the property is vested in the client, or that there are no liens against the property, except as set forth in the title report. Further, most lawyers are not trained to analyze technical or engineering problems and issues.

Opinions about purely factual matters are usually highly qualified, either by limiting the opinions to the lawyer's present actual knowledge, without any independent investigation, or by relying entirely upon the certifications of other professionals, companies, or the client. Opinions qualified in this manner mean only that the lawyer has no actual knowledge contrary to the statements made and, therefore, are of little benefit. Although a lawyer may assist in the analysis of factual matters, for example, by reviewing title data and corporate filings, an opinion should not be used to shift significant business risks of a transaction to the lawyer. In addition, a lawyer's misrepresentation of fact in an opinion may subject the lawyer to liability under a theory of negligent misrepresentation.

The investigation and confirmation of the matters discussed below are generally beyond the scope of legal expertise. However, particular lawyers under particular circumstances may be competent to render opinions about some of the subjects. The following list of subjects is not exhaustive:

1. Blanket Compliance With Laws and Regulations

A lawyer may be asked to give an opinion that a company's business or a particular project is in compliance with all applicable statutes, rules, regulations, judgments, decrees, orders, franchises, or permits. Such an opinion requires the lawyer to have knowledge as to whether numerous facts exist or do not exist and also requires the lawyer to have expertise in many specialized legal subjects ordinarily beyond the scope of the client's requested legal representation. Rarely is the scope of due diligence and legal research necessary to render this type of opinion possible on an economic or timely basis. Thus, the Committee recommends that this type of opinion be avoided.

2. Zoning, Health and Safety, Subdivision, and Environmental Laws and Regulations

A lawyer may be asked for an opinion that a business or project complies with applicable zoning, health and safety, subdivision, or environmental laws and regulations. A comprehensive opinion addressing these matters requires knowledge of, or an intensive investigation to determine, purely factual matters. These matters include: the measurement of setbacks, building heights, and parking spaces under the zoning laws; the adequacy of sprinkler systems, fire walls, and ventilation under health and safety laws; the size of lots, the sufficiency of water supplies, and the cost of assessments or improvements under the subdivision laws; the adequacy and accuracy of soil tests and geological surveys; construction issues under both

building and zoning codes; and the history and use of property and adjoining properties under environmental laws. Lawyers who specialize in these matters may have the expertise to render specific limited opinions in one or more of these areas. Even specialists, however, usually confine their opinions to specific questions of law or to the application of law to known and stated facts, and do not render opinions that address or re-state purely factual matters.

Opinions about these matters are not necessary in most circumstances because less costly or more effective alternatives are available, such as a zoning endorsement from a title insurance company, or a zoning letter from a municipality. Representations and warranties in transactional documents may be used to allocate liability to the appropriate party. A party may provide certificates of technical experts and/or copies of governmental approvals and permits.

3. Title or Priority Matters

Arizona lawyers customarily do not render opinions regarding title to property or the priority of liens. Instead the parties to a transaction usually rely on policies of title insurance issued by title insurance companies, or on UCC searches. In addition, title companies recently have begun issuing UCC insurance policies insuring the priority of some liens covered by the UCC.

To give a proper title opinion for real property, a lawyer must ascertain whether the legal description of the real property is correct and sufficient. The lawyer must also analyze the relevant documents in the chain of title and conduct an extensive search of public records, including court files, probate records, and other governmental files. Almost no Arizona lawyers have the expertise necessary to undertake an extensive abstracting investigation or to ascertain whether the legal description of the real property is correct and sufficient. The preparation and review of legal descriptions is normally performed by a licensed land surveyor.

Title to real property and lien priority are often affected by matters that do not appear in public records. The existence and priority of mechanic's liens, for example, involve issues such as when work commenced or was completed.

An opinion about title to real property or lien priority must address these inherently factual matters. Title companies are usually willing to insure title to property and lien priority—even though title or priority could be affected by off-record matters.

The Illustrative Opinion contains a form of opinion that addresses the proper documentation to evidence the creation of liens encumbering

personal property. However, title and lien priority present significant problems when personal property is involved. Generally, such opinions are heavily qualified because ownership of most personal property cannot be established or traced with any certainty. In addition, the UCC and other statutes establish many off-record lien priorities. Consequently, except for opinions about the sufficiency of instruments, personal property title opinions, and priority of lien opinions are often inappropriate, and the Committee recommends that they be avoided except in special circumstances. Alternatives include obtaining newly-offered UCC insurance from certain title insurance companies.³¹³

4. Fraudulent Transfer or Conveyance

A lawyer should be very careful in giving an opinion to the effect that a certain transaction will not result in a fraudulent transfer or conveyance. To do so, a lawyer would be required to rely almost entirely on certificates or assumed facts because the lawyer would most likely not be in a position to verify or make a determination as to key facts and circumstances, including the client's intent to defraud creditors and the client's solvency. Because the opinion would need to be highly qualified, its value would be limited, and hence, the rendering of such an opinion should be avoided.

5. Licensing and Qualification of the Lender

A lawyer for a borrower may be requested to render an opinion that the lender is not required to obtain a license or to qualify to transact business in order to extend a loan. Such an opinion requires the lawyer to have knowledge as to whether numerous facts exist or do not exist with respect to the lender, a non-client, and requires the lawyer to have special expertise with respect to licensing issues. Thus, the Committee recommends that this type of opinion be avoided.

6. Income Taxation/Tax Liability

A lawyer also may be asked to render an opinion on matters related to a borrower's or lender's actions regarding tax consequences or liabilities including, but not limited to, income taxation. Unless the lawyer: (i) specializes in taxation, (ii) has already undertaken all of the necessary due diligence related to the specific tax liability or action taken by the party addressed in the opinion, and (iii) limits such opinion to a matter regarding a specific tax consequence or liability. An opinion related to general tax

313. See *supra* Section II.B.8.e.

matters is not commonly given and should be avoided. Rarely does time allow for such a review of an entity's records even to opine on a very discreet tax issue. Issues related to taxes and tax liability are overwhelmingly factual in nature, and these opinions are most often obtained from accounting firms specializing in tax advice of this type and are not included in the opinion.

7. Opinions Regarding Regulation T, X, or U of the Board of Governors of the Federal Reserve System

A lawyer may be asked to give an opinion that states that use of the proceeds of a loan will not violate Regulations T, U, and X of the Board of Governors of the Federal Reserve System, 12 C.F.R. sections 220, 221 and 224, respectively. Essentially, these regulations establish rates governing the amount of credit that may be extended as a security (other than exempt securities), the extensions of credit by certain broker-dealers, banks, and other lenders, and the prohibition of obtaining certain types of credit to purchase or carry securities. Unless a lawyer is quite familiar with the intricacies of these regulations (and their exemptions) and is knowledgeable with the due diligence necessary to give such an opinion, an opining lawyer should not give this opinion.

8. Investment Company Status

In securities transactions, an opining lawyer is often asked to provide an opinion regarding a determination of whether the client is an investment company or an entity controlled by an investment company under the Investment Company Act of 1940, as amended (the "Investment Company Act"). If the lawyer's experience does not include an in-depth background regarding the Investment Company Act, a lawyer can overlook the implications of a client's past actions that may make the client an investment company for purposes of the Investment Company Act. Thus, this opinion should be avoided by lawyers who do not possess the requisite knowledge of the Investment Company Act.

B. Legal Uncertainties

A lawyer should neither render nor request an unqualified opinion about issues subject to substantial legal uncertainty. If a proposed transaction (or a portion thereof) is subject to substantial legal uncertainty, the lawyer should so inform the client and, if appropriate, other parties to the transaction so that the parties can make informed business decisions about the transaction.

Opinions about issues subject to substantial legal uncertainty are often heavily qualified, or reasoned. In a reasoned opinion, the lawyer indicates that the law is not settled on a particular issue, discusses statutory and judicial authorities, and predicts how the issue may be decided if properly presented to a court. In many cases, a reasoned opinion serves to inform the recipient about unsettled law, but does not provide significant comfort about a desired result. For this reason, it is often preferable for each party to rely on the advice of its own lawyer about issues subject to substantial legal uncertainty.

1. Material Litigation

Lawyers are often asked to opine as to the absence or existence of material litigation. The problem inherent in such opinions is that the lawyer is required to assess and render a judgment as to the probability of a certain outcome and the results flowing from such outcome at a time when substantial legal uncertainties are involved. This is particularly true where a lawsuit is in the very early stages. Due to the substantial legal uncertainties involved, the absence or existence of material litigation may be an inappropriate topic for an opinion.

2. Covenants Not to Compete

In business transactions, lawyers are often asked to render an opinion that all of the documents signed in a particular transaction are enforceable and/or do not violate any laws. When covenants not to compete are included in such transaction documents, such documents should be excluded from the lawyer's opinion. The legal consequences of the attempted enforcement of a covenant not to compete are often heavily fact based, in some cases hinging on facts and circumstances that arise only after the transaction is completed, and are not consistent from industry to industry. In addition to refusing to enforce certain covenants not to compete, courts may use their authority to remove language from the covenants not to compete to make them enforceable.³¹⁴ Because of the legal uncertainty involved in an opinion that a covenant not to compete is enforceable, lawyers should not be asked to render such an opinion.

314. See *Valley Med. Specialists v. Farber*, 982 P.2d 1277, 1286 (Ariz. 1999); *Varsity Gold, Inc. v. Porzio*, 45 P.3d 352, 354–56 (Ariz. Ct. App. 2002).

C. Opinions About Laws of Foreign Jurisdictions

With certain limited exceptions, a lawyer should not render an opinion about the law of a jurisdiction in which the lawyer is not licensed to practice.³¹⁵ For example, it is usually inappropriate for a lawyer to render an opinion that a business entity is qualified to do business as a foreign corporation in all jurisdictions in which it is required to be qualified. If a party requires an opinion about the law of another jurisdiction, a lawyer licensed to practice in that jurisdiction should be retained.

Lawyers are often asked to render opinions about documents that state that they are to be governed by the laws of another jurisdiction. In many instances, the party requesting the opinion is unwilling to bear the expense of retaining an additional lawyer and will seek comfort from the lawyer already familiar with the documents. Under these circumstances, the lawyer to whom the request is directed has alternatives. These alternatives are discussed in more detail in Section II.B.8.b. of this Report and are as follows: (1) assume, notwithstanding the express terms of the documents, that Arizona law will govern the documents, or (2) render an opinion that the choice of law provisions of the documents are valid, but express no opinion about the enforceability of the documents.

The first alternative has the same practical effect of giving comfort about the legal effect of the documents under Arizona law. Often, this is exactly the assurance sought by the party requesting the opinion, because the requesting party is often already familiar with the legal effect of the documents under the laws of the other jurisdiction. However, the first alternative suffers from the disadvantage that it requires an assumption that is contrary to the intent of the parties.

If rendering an opinion under the first alternative is necessary, the opinion should clearly state the assumptions made. The opinion may state:

The Documents indicate that they are to be governed by the laws of the State of _____. We have no knowledge of those laws and express no opinion thereon. Irrespective of the law which is ultimately determined to apply to the Documents, however, if the Documents were governed by Arizona law, then our opinions set forth above would remain unchanged.

315. See *supra* Section II.A.2 (discussing jurisdictional limitations). It is not uncommon for a lawyer who is familiar with the laws of Delaware or Nevada to render an opinion regarding Delaware or Nevada corporate, limited partnership, or limited liability company law, or Delaware or Nevada UCC perfection law even though the lawyer is not licensed to practice in Delaware or Nevada.

The opining lawyer would then typically include a standard enforceability opinion. This approach requires the opining lawyer to examine the documents in question as though they would be controlled by and enforced under Arizona law (presumably any contrary or questionable provisions will be excluded from the scope of the opinion). It also provides the recipient with some comfort that if a court were to refuse to honor the specific choice of law provisions in the documents and apply Arizona law instead, the documents would nevertheless be enforceable under Arizona law. This approach may also include a separate opinion that the Arizona courts likely will enforce the choice of law provisions, as written.

The second alternative is preferable because it requires no hypothetical opinions. However, a conflict of laws opinion generally requires substantial due diligence and, because it does not address the substantive provisions of the documents, it does not give the party receiving the opinion the desired assurance about the substantive provisions of the documents. If a conflict of laws opinion is given, it may provide:

You have requested that we advise you whether an Arizona court would give effect to the choice of law provision in the Agreement in favor of the law of the State of _____. The Supreme Court of Arizona has consistently ruled that where it is not bound by a previous decision or by legislative enactment, it will follow the rules in the Restatements of the Law, including, without limitation, the Restatements of Conflict of Laws. *Cardon v. Cotton Lane Holdings, Inc.*, 173 Ariz. 203, 841 P.2d 198 (1992); *Taylor v. Sec. Nat'l Bank*, 20 Ariz. App. 504, 514 P.2d 257 (1973); *Burr v. Renewal Guar. Corp.*, 105 Ariz. 549, 468 P.2d 576 (1970); *W. Coal & Mining Co. v. Hilvert*, 63 Ariz. 171, 160 P.2d 331 (1945); *Smith v. Normart*, 51 Ariz. 134, 75 P.2d 38 (1938); and *In re Levine*, 145 Ariz. 185, 700 P.2d 883 (Ct. App. 1985). Section 187 of the Restatement (Second) Conflict of Laws provides that the parties to a contract may stipulate their choice of law to govern the contract and that the laws of the state chosen will be applied unless (i) the particular issue is one that the parties could not have resolved by an explicit provision in their agreement directed to that issue and (ii) either:

(a) The chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or

(b) Application of the law of the chosen state would be contrary to a fundamental policy of a state that has a materially greater interest than the chosen state in the determination of the particular issue and that, under the rule of Section 188 of the

Restatement (Second) Conflict of Laws, would be the state of applicable law in the absence of an effective choice of law by the parties.

Based on the facts concerning the negotiation of the Documents, [such as the place of negotiation and execution of the Documents being the State of _____] and the terms thereof and considering such other matters as we have deemed relevant, we believe that an Arizona court would give effect to the choice of law provisions in the Agreement in favor of the law of the State of _____, (subject to the application of Arizona law with respect to the enforcement of rights and remedies against [real] property located in Arizona).

D. Customary Provisions

A lawyer may, from time to time, be requested to give an opinion generally to the effect that:

The Loan Documents contain provisions which are customary in Arizona for inclusion in loan documents utilized by sophisticated lenders,

or some variant of the foregoing. The Committee is unaware of any definition or standard of customary provisions in documents in Arizona at this time. Consequently, it is difficult to give or justify such an opinion, given this lack of a basis upon which the opinion may be grounded. One response to such a request may generally be that the enforceability opinion itself will most likely address some issues that may be of concern to the lender. For example, the enforceability opinion would generally hold that the following clauses and/or remedies are enforceable if they are contained within the documents reviewed: ability to seek appointment of a receiver upon a material breach; ability to accelerate the debt upon a material breach; ability to enforce liability under the note upon a material breach; ability to foreclose the security instrument(s) on a material breach; and power of private sale under a properly-drafted deed of trust. Alternatively, requesting counsel may be queried as to particular provisions with which such counsel is concerned and, if contained in the documents and enforceable under Arizona law, specific assurance may be given on those particular issues.

At least one national publication³¹⁶ has discussed “opinions” of this type. Observing that the requested opinion is more properly characterized as a factual statement based on the experience of the opining lawyer, that

316. See ACREL/ABA Guidelines, *supra* note 140.

publication goes on to suggest that an opining lawyer should offer an assurance to the effect that the loan documents do not omit essential remedies that, in counsel's experience, are generally found in similar documents for comparable mortgage loans within the relevant jurisdiction.³¹⁷ A recent symposium presented by the ABA Section of Real Property, Probate and Trust Law, dealing with local counsel opinions in multi-state transactions, also explored this issue and addressed the important ethical issues that the opining lawyer may face when asked to provide such assurances. That is, opining counsel is acting, potentially, in direct conflict with the client's interests when suggesting to the lender that the documents prepared by the lender are somehow insufficient. That symposium also suggests that where the lender is utilizing in-state counsel, the lender's concerns as to the adequacy of its documents should be addressed by the lender's own counsel.³¹⁸

E. Smaller Transactions

Because the rendering of an opinion adds significantly to the legal fees of the parties to the Transaction, in smaller "standard" transactions, opinions should not be required. This is particularly true in cases in which the lawyer rendering the opinion is familiar with the laws of the jurisdiction whose laws govern the transaction documents.

IV. ETHICAL CONSIDERATIONS

In considering the form and content of opinions as addressed in this report, lawyers should also be cognizant of matters pertaining to professional ethics and liability. While case law in other jurisdictions may be helpful in this regard,³¹⁹ the principal resources for Arizona lawyers will

317. *See id.* at § 1.1.b.

318. ABA Section of Real Property, Probate and Trust Law Spring Symposium Real Property Division Program Materials (May 2004).

319. Although in all areas of law Arizona courts constantly look to other state's precedent, Arizona practitioners should take note that the Arizona Supreme Court might tend to be more parochial when the issue involves professional ethics and liability. *Cf. Paradigm Ins. Co. v. Langerman Law Offices*, 24 P.3d 593, 598 n.2 (Ariz. 2001) ("We find it unnecessary to cite and review every jurisdiction's treatment of the dual representation issue as we are not bound by any other state's precedent on a purely state-law matter."). It is difficult to reconcile that statement in *Paradigm* with the same opinion's reliance on the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, as the various Restatements are, after all, an amalgam of other states' precedents. *Id.* at 596-97, 600.

be the Arizona Rules of Professional Conduct³²⁰ and the Restatement Third of the Law Governing Lawyers.³²¹ Both authorities deal generally with evaluations (of which an opinion is but one type), and the Restatement expressly addresses opinions in several respects.³²²

A. Relationship to Client

Opinions impinge on ethical and liability aspects of the lawyer-client relationship in ways that are primarily procedural.

1. A Commonplace Process in Legal Practice

First, providing a nonclient with an opinion as to a client is not inherently inconsistent with the lawyer-client relationship. The amount of commentary on opinions in itself evidences that opinions are a commonplace.³²³

2. Identification of the Client

Second, the rendering of the opinion presupposes that the lawyer has a client.³²⁴ A lawyer thus should have a clear understanding of who is the

320. See generally ARIZ. RULES OF PROF'L CONDUCT (2004).

321. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS (2000), of course, did not exist at the time of the 1989 *Report*, *supra* note 2. The RESTATEMENT "is independently important as a contribution to the norms of the legal profession, standing beside the . . . Rules of Professional Conduct." RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, at xxi. The Supreme Court of Arizona has already looked to the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS for guidance in matters of professional responsibility. See *Paradigm Ins. Co.*, 24 P.3d at 596. The Supreme Court of Arizona has consistently ruled that it will look to the RESTATEMENT governing various legal topics in the absence of Arizona statutes or case law addressing an issue. See *Cardon v. Cotton Lane Holdings, Inc.*, 841 P.2d 198, 201–03 (Ariz. 1992); *Burr v. Renewal Guar. Corp.*, 468 P.2d 576, 577 (Ariz. 1970); *W. Coal & Mining Co. v. Hilvert*, 160 P.2d 331, 334–35 (Ariz. 1945); *Smith v. Normart*, 75 P.2d 38, 42 (Ariz. 1938); *Taylor v. Sec. Nat'l Bank*, 514 P.2d 257, 260–61 (Ariz. Ct. App. 1973).

322. In the terminology of professional responsibility, a legal opinion is an "evaluation" provided to a "nonclient." The three principal types of evaluations are audit response letters, reports on internal investigations, and third-party legal opinions. ARIZ. RULES OF PROF'L CONDUCT ER 2.3 (Evaluation for Use by Third Persons); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. a.

323. See *infra* Bibliography, as well as the relevant sections, comments, and reporter's notes of the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS.

324. See, e.g., ARIZ. RULES OF PROF'L CONDUCT ER 2.3 (stating that lawyer may undertake an evaluation of a matter affecting a "client" for the use of a nonclient where compatible with "the lawyer's relationship with the client"); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95(1) (stating that lawyer may provide evaluation "[i]n furtherance of the objectives of a client in a representation").

lawyer's client.³²⁵ In other words, from an ethical perspective, the lawyer should be able to state in a simple sentence the identity of the client. That exercise also has a practical aspect in the case of opinions: the very first sentence of an opinion typically recites the name and nature of the client.³²⁶ The practitioner will have difficulty penning the sentence unless the identity of the client is clear. The opinion, thus, also has an evidentiary aspect. It constitutes the lawyer's statement as to who is the lawyer's client. Accordingly, a lawyer rendering an opinion should consider checking that the client identified in the retention letter is the same client identified in the opinion.

Of course, a lawyer might happen to represent more than one person in connection with a transaction.³²⁷ In the context of a transaction involving an entity such as a corporation, a limited liability company, or a partnership, the lawyer might represent not only the entity but also one or more constituents, such as a shareholder (especially if the transaction involves a parent and one or more wholly-owned subsidiaries).³²⁸ It is entirely permissible for the lawyer to do so provided it is done consistently with the ethical rules. The opinion need not recite the name of every person whom the lawyer has represented in connection with the Transaction, unless the lawyer believes that circumstances warrant recitation or other disclosure of such additional representation in the body of the letter.

3. Generally No Requirement for Client Consent

Third, the lawyer must consider if and to what extent the client should evidence authorization for the rendering of the opinion. Due to a misreading of the Rules of Professional Conduct, it is sometimes assumed that an opinion rendered to a third person must entail some sort of client consent. Such is not the case. The ethical rule requires consent only as to evaluations affecting a client's interests materially and adversely.³²⁹ In this regard, after distinguishing evaluations such as audit-letter-response and internal-

325. ARIZ. RULES OF PROF'L CONDUCT ER 2.3 cmt. 3 ("[I]t is essential to identify the person by whom the lawyer is retained.").

326. See Illustrative Opinion *infra* Appendix A; see also ARIZ. RULES OF PROF'L CONDUCT ER 2.3 cmt. 3, (stating that the identity of the client "should be made clear . . . to others to whom the results are to be made available").

327. See, e.g., ARIZ. RULES OF PROF'L CONDUCT ER 2.2 (Lawyer as Intermediary) (repealed 2003).

328. See, e.g., *id.* ER 1.13 (Organization as Client).

329. *Id.* ER 2.3(b) ("When the lawyer knows or reasonably should know that the evaluation is likely to affect the client's interests materially and adversely, the lawyer shall not provide the evaluation unless the client gives informed consent."); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95(2).

investigation situations (both of which usually deal with disclosure of unpleasant matters), the Restatement notes that third-party opinions in transactions generally advance a client's interest (by facilitating the transaction) and normally benefit clients.³³⁰ In short, the general rule is that third-party opinions do not require the client's consent.³³¹

Thus, the question of client consent for third-party opinions is governed by a specific rule, rather than the general conflict-of-interest rule.³³² Such is the case even though—and probably because—third-party opinions inherently give rise to potential conflicts of interest (as discussed below). The question nevertheless naturally arises as to what the Restatement contemplates by the phrase “material and adverse effect.”³³³ In the context of evaluations generally (including audit letter responses and internal investigations), the principal concern is the disclosure of confidential client information in a way inconsistent with the client's interests, such as by waiving the client's attorney-client privilege or the work-product immunity.³³⁴ Again, however, third-party opinions normally do not involve such a disclosure.

For the rare occasion when a client's authorization might be required for the rendering of a third-party opinion, it is useful for a lawyer to understand the sort of authorization contemplated in this context. When a client's approval is necessary, the Arizona Rules of Professional Conduct require informed consent which is defined in ER 1.0(e).³³⁵

4. Inherent Potential Attorney-Client Conflict

Fourth, as a practical matter both in deciding whether to render an opinion and in connection with preparing an opinion, it is desirable for the lawyer to consider both the short-term and the long-term future of the lawyer-client relationship. Such an exercise is helpful because what was theretofore a bilateral relationship will, on the rendering of the opinion, become a triangular relationship: As discussed below, in rendering an

330. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmts. b, d.

331. *See id.* §§ 21(3), 61.

332. As to the general conflict-of-interest rule, see ARIZ. RULES OF PROF'L CONDUCT ER 1.7, *reprinted in* ARIZ. REV. STAT. ANN., vol. 17A (2004); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 121 (2000). *See also* Paradigm Ins. Co. v. Langerman Law Offices, 24 P.3d 593 (Ariz. 2001) (applying the Arizona rule and the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS).

334. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. d.

335. ARIZ. RULES OF PROF'L CONDUCT ER 1.0(e), ER 2.3(b), *reprinted in* ARIZ. REV. STAT. ANN., vol. 17A (2004) (Informed consent is “the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.”).

opinion to a nonclient, the lawyer might owe certain duties to the recipient of the opinion and thus faces the prospect of being liable to the recipient for breach of duty.

In the short-term, the lawyer's desire to protect against claims by the recipient naturally causes the lawyer to resist giving any opinion. That resistance may cause the lawyer's interests to diverge from the interests of a client who desires to consummate a transaction with a party who insists on receiving an opinion. This difficulty can often be forestalled if the transaction involves a letter of intent or other preliminary outline of points, as the document can make clear that no opinions will be requested of either party in the proposed transaction. That will not always be possible, though.

In the long-term, if the recipient of an opinion later accuses the lawyer of breaching a duty, a strain might be placed on the lawyer-client relationship as the lawyer prepares a defense (especially if in rendering the opinion the lawyer had relied on information provided by the client). Thus, as a practical matter, a lawyer should refrain from volunteering or rendering an opinion to a nonclient unless a good reason exists for rendering the opinion, particularly where the delivery of an opinion is not customary.

5. Liability to Client

Of course, in addition to those procedural aspects of an opinion on lawyer-client interaction, there is also a substantive aspect of opinions in the context of the lawyer-client relationship: it is possible that, if a client alleges injury due to a lawyer's purported negligence in providing an opinion, the client might claim that the lawyer has liability to the client.³³⁶ The nature of such claims is beyond the scope of this Report.

B. Relationship to Nonclient (the Recipient of the Opinion Letter)

1. The Evolving Duty of the Opining Lawyer

The comment to the Arizona ethical rules says that the opining lawyer "may or may not" have a legal duty to the recipient, but goes on to say that the matter is "beyond the scope of this Rule."³³⁷ From an ethical perspective, thus, the only clear admonition is that the lawyer must not

336. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 95 cmt. a, 51 cmt. e.

337. ARIZ. RULES OF PROF'L CONDUCT ER 2.3 cmt. 4 ("[A] legal duty . . . may or may not arise.").

knowingly “make a false statement of material fact or law to a third person.”³³⁸

From the perspective of an opining lawyer’s potential liability to the recipient, the Restatement provides that the opining lawyer is obligated to exercise care to a certain extent in rendering the opinion and “not make false statements” in rendering the opinion.³³⁹ The Restatement comment clarifies that there is really only one duty that the opining lawyer owes to the recipient: that duty is to provide a “fair and objective” opinion.³⁴⁰

“Objectivity” simply means that the opining lawyer “does not function as an advocate for the legal or factual position of the lawyer’s client.”³⁴¹ Litigation pleadings and briefs are by nature advocative and conclusory, admitting of no doubt as to the client’s position and right to ultimately prevail. As discussed throughout this Report, an opinion has a different function. Indeed, the discussion below regarding limitations and qualifications in opinions evidences that the ethical rules expect opinions to acknowledge doubts and reservations.

“Fairness” means that the opining lawyer must not make false representations in the opinion.³⁴² As the Restatement says, “the duty of a lawyer providing an opinion is ordinarily limited to using care to avoid making or adopting misrepresentations.”³⁴³ In the context of opinions, this requirement (spelled out in Section 98 of the Restatement) is that the opinion not “knowingly make a false statement of material fact or law to the nonclient.”³⁴⁴ The Restatement acknowledges that, insofar as false statements in opinions are concerned, Section 98 rather than Section 51 (which is not qualified by “knowingly”) controls, and that the lawyer’s duty is thus less extensive than is otherwise the case in dealings with nonclients.³⁴⁵

As such, in Arizona, with respect to “evaluations” generally and opinions specifically (as opposed to other areas of professional liability), the liability

338. *Id.* ER 4.1(a); *see* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 95 cmt. a, 98; *see also* ARIZ. RULES OF PROF’L CONDUCT ER 8.4(c) (stating that misconduct includes “dishonesty, fraud, deceit or misrepresentation”); *In re* Duckworth, 914 P.2d 900, 901 (Ariz. 1996) (invoking Rules of Professional Conduct 4.1 and 8.4 in context of legal opinion). The notion of “competence” does not apply to the opining lawyer-recipient relationship; rather, it extends only to the client. *See* ARIZ. RULES OF PROF’L CONDUCT ER 1.1 (requiring “competent representation to a client.” (emphasis added).

339. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95(3).

340. *Id.* § 95 cmt. c.

341. *Id.*

342. *See id.* §§ 95 cmts. a & c, 51 cmt. e, 56 cmt. f, 98 cmt. b.

343. *Id.* § 51 cmt. e.

344. *Id.* § 98(1); *see also id.* § 95 cmt. c.

345. *Id.* § 95 cmt. c.

standard appears to require that a misstatement of fact or law in an opinion be knowing, and not merely reckless or negligent.³⁴⁶ This special rule as to misstatements in connection with opinions may be an acknowledgment of the reality that, while an opining lawyer is expected to be objective in rendering an opinion, the lawyer nevertheless “will be understood by nonclients to be making nonimpartial statements.”³⁴⁷

Despite this one limited duty to a recipient, the opinion does not cause the recipient to become a client of the opining lawyer and, thus, concomitant duties such as confidentiality do not attach.³⁴⁸ In addition, other than addressing the specific issues set forth in the opinion, the opining lawyer does not undertake to advise the recipient on any aspect of the transaction. For example, the opining lawyer has no obligation to comment on whether the transaction is in the recipient’s best interest, whether the transaction should be structured differently, or whether certain terms of the transaction documents should be changed.³⁴⁹ However, if the lawyer invites the recipient to rely on the lawyer to provide services other than furnishing the opinion, the lawyer may have incurred other duties, including the duties of a lawyer-client relationship.³⁵⁰

346. *Id.* § 98 cmt. c. This is consistent with the “knowingly” standard articulated by ARIZ. RULES OF PROF’L CONDUCT ER 4.1(a) (“In the course of representing a client a lawyer shall not knowingly make a false statement of material fact or law to a third person.”).

The comments to sections 95 and 98 of the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS, make cross-references to Section 51, which deals generally with a lawyer’s duties to nonclients (with third-party legal opinions being only one occasion for such a duty). RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 95, 98. Section 51, comment e, distinguishes between negligent and intentional misrepresentation. *Id.* § 51 cmt. e. The latter comment also appears to indicate that a standard of intentional misrepresentation applies in the case of legal opinions. *Id.* § 98; *see also id.* § 56 cmt. f (noting that “[a] lawyer is liable for negligent misrepresentation to a nonclient in the course of representing a client only when the lawyer owes the nonclient a duty of care under § 51” but referring to § 95 as to legal opinions specifically).

Paradigm Ins. Co. v. Langerman Law Offices is a case that did not involve third-party legal opinions (or other “evaluations”), and is thus consistent with the interpretation set forth in the text regarding legal opinions. 24 P.3d 594 (Ariz. 2001). Here, the Arizona Supreme Court viewed section 51 of the RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS as applicable and referred to the section as embodying a “negligence” standard in certain non-opinion contexts. *Id.* at 600–02.

347. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 98 cmt. c.

348. *Id.* § 95 cmt. c.

349. *See id.* (a lawyer has no duty to advise a third party as to whether a real estate transaction should proceed, whether title should be taken in a different form, or whether other terms should be altered).

350. *Id.*

2. Ramifications for the Opinion Letter

These concepts basically translate into clarifying the limited nature of the opinion in the opinion itself. Otherwise, the lawyer runs the risk of having the limits in the scope of the opinion dictated by reference to “customary practice” (such as the precepts set forth in this Report) or “reasonableness”—limits that may or may not correspond with those intended by the lawyer. In this regard, lawyers need to think of themselves as not only diligent, but also vigilant. If asked about the most troubling aspect of an opinion, opining lawyers might often say that they are most concerned about the nature and extent of the law supporting a legal conclusion. The concern should be elsewhere: the very real possibility of representing a dishonest—or, at least, less than candid—client.

An opining lawyer typically will be cognizant of the lawyer’s own duty to not knowingly make a false statement as discussed earlier. The lawyer naturally wants to assume that a transactional client also acts in good faith, but the law of lawyering recognizes that not all clients do so. Thus, the opining lawyer cannot assist a client in a crime or fraud,³⁵¹ and the opining lawyer also has certain obligations if the lawyer learns that the client has committed or intends to commit a crime.³⁵² However, whether a client has issues with facts is not always obvious. Sometimes the matter might come to the lawyer’s attention in a benign way, as when the client notes a certain representation in a proposed agreement and asks whether a particular matter is covered by the representation. Or the client might be in a hurry to consummate a transaction and orally represent to the opining lawyer that the requisite approval by the board of directors was obtained, when in fact the client is assuming that the board will ratify the action. In other situations, the client might simply remain silent despite knowledge that the opining lawyer is reviewing an incomplete set of documents.

An opining lawyer can avoid both unwarranted interpretation of the opinion and implied endorsement of client misconduct by having the opinion be clear as to (a) the investigation conducted in preparing the opinion, (b) the factual basis of the opinion, (c) material assumptions made for purposes of the opinion, and (d) material limitations and qualifications to which the opinion is subject. These matters are discussed at length in other parts of this Report,³⁵³ but certain ethical and liability ramifications are noted here.

351. ARIZ. RULES OF PROF’L CONDUCT ER 1.2(d).

352. *Id.* ER 1.6(b)–(c).

353. *See supra* Parts II.A., C.–D.

a. Investigation

As to the underlying investigation, customary practice (such as the precepts set out in this Report) will determine the nature and extent of the legal and factual diligence to be employed by the lawyer giving the opinion, except as stated in the opinion or otherwise agreed.³⁵⁴ Therefore, the opinion implies that the lawyer's investigation was consistent with customary practice and otherwise reasonable in light of, among other circumstances, the parties' understanding, the ascertained facts, the likelihood of the nonclient's reliance on the opinion, and the risks associated with the transaction.³⁵⁵

If the opinion states the limited nature of the investigation (which may be more or less than that required by customary practice) and the facts resulting from that investigation support the opinion, then the lawyer does not violate the duty of care by relying on that stated investigation, even if other investigation would have divulged contradictory information.³⁵⁶ For example, a lawyer might state that an opinion is based solely on a review of a certain document (e.g., a preliminary title report, an officer's certificate, a litigation report) without further investigation.³⁵⁷

b. Factual Basis

The opinion's factual basis is as stated in the opinion. To the extent the factual basis is unstated, the factual basis can be derived by implication from the circumstances. If the opinion recites certain facts, the reader must reasonably assume that the lawyer is merely reporting what the lawyer believes to be accurate. In other words, the opinion's recitation of facts should not be deemed a representation by the lawyer as to the accuracy of those facts. If the recipient has questions about such accuracy, the recipient must make its own judgment about the adequacy of the investigation (addressed elsewhere in the opinion) and whether the recipient is comfortable with that level of investigation. In all cases, the opinion is not a guarantee that the facts are accurate—unless the opinion expressly states otherwise or unless otherwise agreed.³⁵⁸

354. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. e.

355. See *id.* § 95 cmt. c.

356. See *id.*

357. *Id.* § 95 cmt. c, illus. 1.

358. *Id.* § 95 cmt. c.

c. Assumptions

As to material assumptions, the lawyer is entitled to make and rely on assumptions that serve as a predicate to the opinion whether the assumption is implied or stated.³⁵⁹ If an assumption is known by the lawyer to be inaccurate, or if reliance on the assumption is known by the lawyer to be unwarranted, the lawyer may still rely on the assumption, but must expressly disclose the underlying inaccuracy or unreliability—unless already “known by or apparent to” the recipient or the recipient’s counsel.³⁶⁰ To avoid disputes about who knew what or what was apparent, the lawyer should thus consider whether to make the disclosure in writing (either in the opinion or a separate communication) or otherwise memorialize the knowledge of the recipient and the recipient’s lawyer or why the issue should be apparent.³⁶¹

d. Limitations and Qualifications

Material limitations and qualifications may arise as to either the law or the facts. The preferred method of dealing with a limitation or qualification depends on whether it affects certitude regarding a matter of law (such as the legal conclusion expressed by the opinion) or a matter of fact (such as the factual basis of the opinion).

As to matters of law, the lawyer generally is not required to state all possible reservations or doubts about a legal issue. In other words, even in contexts not involving opinions, a lawyer generally will not be liable when erring as to an unsettled area of the law.³⁶²

If, however, the doubts rise to a level that prevents the lawyer from reasonably concluding that the opinion reflects the result that would be reached by the Arizona Supreme Court, the lawyer should refer to doubt or state a reservation.³⁶³

For example, as discussed elsewhere in this Report, review of appropriate documentation may enable an opining lawyer to express an unqualified legal conclusion about an entity’s due formation.³⁶⁴ On the other

359. See *supra* Section II.D.

360. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. c.

361. See *supra* Section II.d (discussing assumptions).

362. See *Talbot v. Schroeder*, 475 P.2d 520, 521 (Ariz. Ct. App. 1970) (citing *Martin v. Burns*, 429 P.2d 660 (Ariz. 1967) and stating that no liability exists when a lawyer errs with regard to an unsettled area of law).

363. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. c (noting that “[t]he lawyer is not required to state reservations or doubts . . . unless they are of a nature that prevents the lawyer from reasonably concluding that the opinion reflects the result that would be reached by the highest court of the applicable jurisdiction.”); *id.* § 51 cmt. e.

364. As to opinions about formation of entities, see *supra* Section II.B.1.

hand, if the issue deals with an interrelationship between two statutes, both of which are arguably applicable but contradictory, and no Arizona court has spoken to the issue, circumstances may warrant having the opinion mention the interpretive difficulty. On questions involving an extremely unsettled area or the balancing of several factors, a reasoned opinion might therefore be more appropriate.³⁶⁵ Examples of very unsettled legal areas might include: the effect of a newly-enacted statute with which no court has yet dealt and about which commentators have expressed diverse views; a matter of common law which would be a matter of first impression in Arizona and as to which the courts of other states have reached no consensus; or an issue that is essentially the same issue pending before an appellate court. An example of an issue entailing analysis of a variety of factors might be the question of the validity of contracting parties' choice of law with respect to enforcement of a certain type of lien or security interest.

The converse applies to matters of fact: significant limitations on the factual bases for the opinion should be stated unless customary practice clearly indicates otherwise.³⁶⁶ For example, if an opinion letter is subject to a limitation or a condition precedent of a factual nature (such as the occurrence of a transaction), the Arizona Supreme Court has said that the limitation or condition should be "expressly stated . . . or specifically described" in the opinion.³⁶⁷ As an example of a customary practice that enables an opinion to dispense with recitation of a limitation, the Restatement's Comment notes that opinions "typically rely as a matter of customary practice" on factual representations in officers' certificates without expressly stating that the investigation of those facts was limited to reading the certificate and determining that the officer was the proper person to address those facts.³⁶⁸

In short, to the extent customary practice (such as the concepts set out in this Report) evidences that certain legal or factual reservations may go unstated, the opinion need not recite them.

3. Internal Review

Neither the law nor ethical principles require that an opinion be reviewed by another lawyer or committee prior to delivery by the opining lawyer. Any other rule would, of course, discriminate against sole practitioners and small firms.

365. Reasoned opinions are discussed *supra* Sections II.B.8.b, III.b, and IV.B.2.d.

366. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. c.

367. *In re Duckworth*, 914 P.2d 900, 901 (Ariz. 1996).

368. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. c.

Use of such a review may, however, have evidentiary value in showing exercise of any requisite standard of care. For that reason (or because a law firm's malpractice insurer recommends it), a law firm might adopt a policy regarding opinion letters. The scope and nature of such policies vary widely. A policy might pertain to all evaluations (including responses to audit response letters, investigation reports, and letters of advice to clients), or might be limited to third-party opinions. Among the procedures that can be (but are not necessarily) found in such policies are review by another partner in the firm and preparation of a memorandum regarding the factual and legal basis for each issue addressed in the opinion.³⁶⁹ As a practical matter, even in the absence of a formal written policy, such review may exist in most firms, where the principal lawyer on, for example, a corporate transaction might look to one or more other lawyers in the firm for assistance on issues involving certain noncorporate areas of the law (e.g., environmental matters, employee benefits, intellectual property, and so on) if the firm has lawyers who focus on those areas.

C. The Nonclient's Lawyer

The lawyer for the recipient of the opinion should also consider certain factors.

First, there is nothing inherently unethical in the recipient's lawyer requesting an opinion from the other party, specifying the matters to be addressed in the opinion, or commenting on and negotiating the details of the opinion. For example, loan agreements commonly condition the making of the loan on receipt of an opinion from borrower's counsel on certain stated matters.³⁷⁰

Second, having the other party's counsel render an opinion does not absolve the recipient's lawyer of the latter's own duty of care. Many legal issues pertinent to a transaction (e.g., usury) depend almost entirely on

369. Several theoretical benefits are often propounded as to such internal procedures, with some of those benefits perhaps being more pertinent simply to prevention of professional embarrassment: the opining lawyer might be so preoccupied with the transaction, either professionally or personally, that objectivity or adequate attention to the details of the opinion could suffer. Centralized review can help build a store of precedent for dealing with various types of opinions. It can also help verify that an area involving specialized knowledge has been reviewed by a lawyer in the firm who practices in that area. The group activity inherent in a review may also help deter unwarranted pressure from a client or a third party as to the rendering of an opinion.

370. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 95 cmt. e ("The details of the opinions . . . are negotiated between the lawyers for both the client and the intended recipient.").

application of the law to the transaction documents—that is, neither the opining lawyer nor the recipient’s lawyer enjoys any inherent advantage over the other as to access to the relevant facts and documents. Indeed, where the recipient’s lawyer is, for example, counsel to a lender and is continually engaged in loan documentation, the recipient’s lawyer may be more knowledgeable than the opining lawyer about many legal issues that might be addressed in an opinion. As a matter of both practicality and civility (if not necessarily of ethics), the recipient’s lawyer should consider whether requesting an opinion on such issues serves any purpose, other than increasing the cost of the transaction to the opining lawyer’s client.³⁷¹ Moreover, if the recipient’s lawyer believes such an issue is of sufficient importance to the recipient, the recipient’s lawyer should consider whether it is in fact in the best interests of the recipient for the recipient’s lawyer (or local counsel retained by the recipient’s lawyer) to be analyzing the issue, instead of (or in addition to) requesting an opinion from the other party’s counsel.

Third, the “golden rule”—limiting requests for opinions from an opposing lawyer to those opinions that the requester would be willing to render—has underpinnings that go beyond mere notions of fair play and civility. For example, if the recipient’s lawyer believes that a requested opinion would be difficult for anyone to give in the context of the transaction and also believes that the opining lawyer may not be sensitive to the difficulty (whether because the recipient’s lawyer is in a unique position to be aware of a material factor of which no one else is aware, because the recipient’s lawyer has no confidence in the opining lawyer’s competence, or is much more experienced in a particular field, or for some other reason), the recipient’s lawyer should consider whether to disclose those concerns to the opining lawyer. Clearly, the recipient’s lawyer should refrain from making misstatements in trying to coax an opinion from the opining lawyer, such as by asserting that a particular opinion is “quite customary” when the recipient’s lawyer knows that such is not the case.³⁷² In any event, if the recipient’s lawyer harbors such reservations about the value or accuracy of

371. See *id.* § 95 cmt. b (stating that evaluations make more sense when it would be “wasteful or impractical” for one party to evaluate a matter when another party is in a position to evaluate it “more readily”).

372. See ARIZ. RULES OF PROF’L CONDUCT ER 8.4(c) (2004) (prohibiting conduct involving dishonesty, fraud, deceit or misrepresentation), ER 4.1 (prohibiting false statements); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 98 (prohibiting false statements to nonclients).

the opinion, the recipient's lawyer should consider whether to disclose those concerns to the client-recipient.³⁷³

373. See ARIZ. RULES OF PROF'L CONDUCT ER 1.4 (communication); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 20 (duty to inform and consult with client).

APPENDIX A

ILLUSTRATIVE OPINION

[LETTERHEAD]

[DATE]

[Name and address of opinion recipient]

RE: Transaction (the “Transaction”) between _____
 (“You”) and _____ (the “Company”)

Ladies and Gentlemen:

We have acted as counsel to the Company in connection with the Transaction evidenced by the Documents (as defined below). You have requested our opinion about certain matters pursuant to Section _____ of the _____ Agreement (as defined below). Capitalized terms used and not otherwise defined in this letter shall have the meanings ascribed to them in the Documents.

As used in this opinion, the phrase “to our knowledge,” or words of similar import, mean, as to matters of fact, that, to the actual knowledge of the attorneys within our firm principally responsible for the Transaction and after an examination of Documents, but without any independent factual investigation or verification of any kind other than inquiries of certain officers of the Company, such matters are factually correct.

[This opinion incorporates by reference, and is to be interpreted in accordance with, the First Amended and Restated Report of the State Bar of Arizona Business Law Section Committee on Rendering Legal Opinions in Business Transactions, dated October 20, 2004.]

For purposes of this opinion, we have examined such questions of law and fact as we have deemed necessary or appropriate. We have examined only the following documents (collectively, the “Documents”) and have made no other investigation or inquiry:

I. Transaction Documents and Other Documents Examined

We have reviewed the following documents (the “[Transaction] [Loan] Documents”), which we received in [draft form] from _____ on [date].

Each of the [Transaction] [Loan] Documents [is to be] [has been] executed by each of the signatory parties thereto and dated as of the Closing Date.

[List all Transaction documents reviewed]

In addition, we have reviewed the following documents (the “[Organizational] [Entity] Documents”).

[List all Organizational documents, including articles, bylaws, resolutions, certificates from public authorities, certificates from officers, etc.]

As to certain matters of fact bearing upon the opinions expressed herein, we have relied on:

- a. A Certificate of the President of the Company, dated _____, 20__;
- b. A Certificate of Good Standing with respect to the Company, dated _____, 20__, issued by _____; and
- c. Information in public authority documents.

II. Opinions

Based on the foregoing, and subject to the assumptions, qualifications, and limitations set forth below, it is our opinion that:

1. (If the Company is a corporation) The Company is a corporation [duly formed] [duly organized], validly existing, and in good standing under the laws of the State of Arizona.

OR (If the Company is a general partnership) The Company is a validly existing Arizona partnership.

OR (If the Company is a limited partnership) The Company is a limited partnership duly organized and validly existing under the Arizona Uniform Limited Partnership Act.

OR (If the Company is a limited liability partnership) The Company is a validly existing [general] [limited] partnership which has qualified as a limited liability partnership.

OR (If the Company is a limited liability company) The Company is a limited liability company validly existing under the laws of the State of Arizona.

OR (If the Company is a foreign corporation) The Company [is a corporation duly organized, validly existing, and in good standing under the laws of the State of _____ and] is qualified to do business as a foreign corporation under the laws of the State of Arizona.

OR (If the Company is a foreign limited partnership) Based solely on the [certificate of limited partnership filing dated _____, 20__, issued by the Arizona Secretary of State] [statement of foreign qualification filed with the Arizona Secretary of State on _____, 20 __], the

Company is qualified to do business as a foreign limited [liability] [liability limited] partnership under the laws of the State of Arizona.

OR (If the Company is a foreign limited liability company) Based solely on the Certificate of Registration issued by the Arizona Corporation Commission on _____, 20 __, the Company is qualified to do business as a foreign limited liability company under the laws of the State of Arizona.

2. (If the Company is a corporation) The Company's authorized capital consists of _____ common shares, of which _____ shares are issued and outstanding. The shares issued [pledged] in the Transaction have been duly authorized and are validly issued, fully paid, and nonassessable.

OR (If the Company is a limited liability company) The Company has received all required capital contributions, and there are no outstanding obligations of the members to make additional capital contributions to the Company.

3. The execution, delivery, and performance of the Documents by the Company have been duly authorized by all requisite corporate [limited liability company] [partnership] action on the part of the Company.

4. The Documents have been duly executed and delivered by the Company.

5. The Company has the requisite corporate [limited liability company] [partnership] power and corporate [limited liability company] [partnership] authority to: (i) own and operate its properties and assets [the properties and assets described in _____]; (ii) carry out its business as such business is currently being conducted [as described in _____]; and (iii) carry out the terms and conditions applicable to it under the Documents.

6. [Based solely upon our knowledge and the representations of the Company [in the Agreement] OR [in an officer's certificate delivered to us dated _____]],

OR [Based solely upon [our examinations as of _____, _____, of the records of the filings in the Superior Court of _____ and United States District Court for the District of Arizona, [and _____] from _____, _____, through _____, _____, [our knowledge,] and the representations of the Company],

OR [Based solely upon [our review of the results of the litigation search dated _____, _____ performed by _____] [our review of an Affidavit of the Clerk of the _____ County Superior Court/United States District Court for the District of Arizona], we have no

knowledge of any [material] pending [or overtly threatened (in writing and delivered to opining lawyer)] litigation, arbitration, mediation, or other alternative dispute resolution proceeding against the Company that will negatively affect the transaction or that will have a materially adverse effect on the Company [except _____].

7. No consent, approval, authorization, or other action by, or filing with, any federal, state, or local governmental authority is required in connection with the execution and delivery by the Company of the Documents and the consummation of the Transaction [or, if any of the foregoing is required, it has been obtained].

8. The execution and delivery of the Documents and consummation of the Transaction by the Company will not violate the Company's [articles of incorporation], [articles of organization], [certificate of limited partnership], [bylaws], [operating agreement], or [partnership agreement].

9. [Based solely upon our knowledge,] the execution and delivery of the Documents and consummation of the Transaction by the Company will not violate any judgment, order, or decree of any court or governmental agency to which the Company is a party or by which it is bound.

10. [Based solely upon our knowledge,] [and a review of those material agreements disclosed to us by the Company on the [attached] officer's certificate dated _____, _____,] the execution and delivery of the Documents and consummation of the Transaction by the Company will not cause a breach or default of such material agreements.

11. The execution and delivery of the Documents and consummation of the Transaction by the Company will not violate any applicable law, rule or regulation affecting the Company.

12. The Documents are valid, binding, and enforceable obligations of the Company.

13. Based upon decisions of the Supreme Court of Arizona and applicable Arizona statutes, we believe the courts in Arizona will honor the choice of law clause(s) in the Documents. *See* Restatement (Second) of Conflict of Laws, sections 187, 188, 203 and 229, cmt. e (1971); *Cardon v. Cotton Lane Holdings, Inc.*, 173 Ariz. 203, 205–09, 841 P.2d 198, 200–04 (1992); *Burr v. Renewal Guar. Corp.*, 105 Ariz. 549, 550, 468 P.2d 576, 581 (1970); A.R.S. sections 47-1105(A) and 47-9301–47-9307 (UCC RA9).

OR You have requested that we advise you whether an Arizona court would give effect to the choice of law provision in the Documents in favor of the law of the State of _____. The Supreme Court of Arizona has consistently ruled that where it is not bound by a previous decision or by legislative enactment, it will follow the rules in the Restatements of the Law, including, without limitation, the Restatements of Conflict of Laws.

Smith v. Normart, 51 Ariz. 134, 75 P.2d 38 (1938); *W. Coal & Min. Co. v. Hilvert*, 63 Ariz. 171, 160 P.2d 331 (1945); *Burr v. Renewal Guar. Corp.*, 105 Ariz. 549, 468 P.2d 576, (1970); and *Taylor v. Sec. Nat. Bank*, 20 Ariz. App. 504, 514 P.2d 257 (1973); *In re Levine*, 145 Ariz. 185, 700 P.2d 883 (Ct. App. 1985); *Cardon v. Cotton Lane Holdings, Inc.*, 173 Ariz. 203, 841 P.2d 198 (1992). Section 187 of the Restatement (Second) Conflict of Laws provides that the parties to a contract may stipulate their choice of law to govern the contract and that the laws of the state chosen will be applied unless (i) the particular issue is one that the parties could not have resolved by an explicit provision in their agreement directed to that issue and (ii) either:

(a) The chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or

(b) Application of the law of the chosen state would be contrary to a fundamental policy of a state that has a materially greater interest than the chosen state in the determination of the particular issue and that, under the rule of section 188 of the Restatement (Second) Conflict of Laws, would be the state of applicable law in the absence of an effective choice of law by the parties.

Based on the facts concerning the negotiation of the Documents, [such as the place of negotiation and execution of the Documents being the State of _____] and the terms thereof and considering such other matters as we have deemed relevant, we believe that an Arizona court would give effect to the choice of law provisions in the Documents in favor of the law of the State of _____, (subject to the application of Arizona law with respect to the enforcement of rights and remedies against [real] property located in Arizona).

AND/OR The Documents indicate that they are to be governed by the laws of the State of _____. We have no knowledge of those laws and express no opinion thereon. Whichever law is ultimately determined to apply to the Documents, however, if the Documents were governed by Arizona law, then our opinions set forth above would remain unchanged.

14. The [guarantee document] as drafted is enforceable against the signer's sole and separate property, but is not enforceable against the marital community or the community property [pursuant to A.R.S. section 25-214].

15. The [security agreement document] is sufficient to create in favor of the Lender a security interest in any rights of the Company in the described collateral in which a security interest can be created under Article 9 of the Uniform Commercial Code ("UCC").

16. The fixture financing statement [or the deed of trust, or both] is [are] in proper form for filing with the office of the county recorder and, upon due filing in such office, will constitute a “fixture filing” under the UCC with respect to any fixtures described therein. The central financing statement is in proper Arizona form for filing with the office of the Arizona Secretary of State and, upon due filing in such office, will perfect a security interest in that collateral described therein as to which a security interest has been duly granted to Lender by the Company and to the extent a security interest can be perfected in such collateral under the Arizona UCC by the filing of a financing statement in the office of the Arizona Secretary of State.

17. The deed of trust [mortgage] is sufficient in form to create a valid lien in favor of the Lender upon the Company’s interest in the real property described therein and to be recorded in the real property records of the county recorder of the county in which the property is located [, and upon recordation will impart constructive notice of the lien to third parties].

18. The provisions of the security agreement are effective to create a valid security interest in that portion of the collateral consisting of federally-registered copyrights, common law copyrights, trademarks or service marks, or applications for any such marks, and patents, to the extent that (a) the borrower has rights in such collateral, and (b) a security interest in such collateral may be granted pursuant to Article 9 of the UCC. Under current law, upon the filing of the UCC1 Financing Statement in the manner described above, it appears that all action necessary to perfect a security interest in such collateral (with the exception of federally-registered copyrights) will have been taken. Regarding federally-registered copyrights, under current law, upon the recording of the transfer with the United States Copyright Office, it appears that all action necessary to perfect a security interest in federally-registered copyrights will have been taken. The federal statutes governing trademarks and patents do not set forth the procedure for perfection and priority of liens encumbering trademarks and patents in the same detail as in the United States Copyright Act. Accordingly, certain courts have reached the conclusion that the Lanham Act and the Patent Act do not preempt state law and that recordation of a security interest with the United States Patent and Trademark Office is not required to perfect an otherwise valid security interest. *In re Cybernetic Servs, Inc.*, 239 B.R. 917, 920 (B.A.P. 9th Cir. 1999); *In re Together Dev. Corp.*, 227 B.R. 439, 441 (Bankr. D. Mass. 1988); *In re TR-3 Indus.*, 41 B.R. 128, 131 (Bankr. C.D. Cal. 1984). However, there is no guarantee that filing the UCC1 Financing Statement in the manner described above alone will be sufficient in the

future to maintain a perfected security interest in patents, federally-registered trademarks or service marks or applications for such marks.

19. We have been asked to render our opinion as to whether, in the event that [non-SPE Affiliate] (the “Affiliate”) were to become a debtor in a case under Title 11 of the United States Code (the “Bankruptcy Code”), a court of competent jurisdiction, exercising reasonable judgment after full consideration of all relevant factors, in a properly presented and argued case, would recognize the separate existence of the Borrower, on the one hand, and the Affiliate, on the other hand, and accordingly, would not order the substantive consolidation of the assets and liabilities of the Borrower with those of the Affiliate.

20. Based on the foregoing, and subject to the assumptions, qualifications and discussions contained herein and the reasoned analysis of analogous case law, it is our opinion that, in the event that [Non-SPE Affiliate] were to become a debtor in a case under the Bankruptcy Code, in a properly presented and argued case, a court of competent jurisdiction would recognize the separate existence of borrower and [Non-SPE Affiliate], and, accordingly, would not order the substantive consolidation of the assets and liabilities of borrower and [Non-SPE Affiliate].

III. Assumptions

With your permission, in rendering the foregoing opinions, we have made the following assumptions. We have made these assumptions without independent verification, and with the understanding that we are under no duty to inquire or investigate regarding such matters; [however, we have no knowledge of any facts that we know to be inaccurate or any factual representations that we know to have been provided under circumstances making reliance unwarranted.]

a. The genuineness of the client’s signatures not witnessed, the authenticity of documents submitted as originals, and the conformance to originals of documents submitted as copies.

b. That each client who is a natural person, and who is executing any of the Documents or otherwise involved in the Transaction, possesses the legal competency and capacity necessary for such individual to execute such documents and/or to carry out such individual’s role in the Transaction.

c. The Documents are valid, binding, and enforceable obligations of the parties thereto in accordance with their respective terms. [To be used when another lawyer renders an opinion that the Documents are enforceable.]

d. The Documents accurately and completely describe and contain the parties' mutual intent, understanding, and business purposes, and that there are no oral or written statements, agreements, understandings, or negotiations, nor any usage of trade or course of prior dealing among the parties, that directly or indirectly modify, define, amend, supplement, or vary, or purport to modify, define, amend, supplement, or vary, any of the terms of the Documents or any of the parties' rights or obligations thereunder, by waiver or otherwise.

e. The applicable Documents, immediately after delivery, will be properly filed or recorded in the appropriate governmental offices, that You will timely file all necessary continuation statements, and that all fees, charges, and taxes due and owing as of this date have been paid. [For use where the opining lawyer is not responsible for recordation or filing]

f. The result of the application of Arizona law as specified in the Documents will not be contrary to a fundamental policy of the law of any other state with which the parties may have material or relevant contact in connection with the Transaction and as to which there is a materially greater interest in determining an issue of choice of law. [For use in an enforceability opinion, where the documents recite an Arizona choice of law, and if choice of law is not expressly excluded from the opinion]

g. You will receive no interest, charges, fees, or other benefits or compensation in the nature of interest in connection with the Transaction other than those that the Company (and, where applicable, the guarantor) has agreed in writing in the Documents to pay. [For use in a loan transaction, in light of the language of A.R.S. sections 44-1201, 44-1202]

h. In connection with our opinion in paragraph 2 above concerning the due authorization of the shares, our investigation revealed that certain corporate records concerning [specify the missing records and describe their relevance] were either missing or incomplete. As a result, we have relied on the presumption of regularity and continuity to the extent necessary to enable us to provide that opinion.

i. That the Company has paid all income taxes, fines, jeopardy, or fraud assessments, and interest due from it and payable to the State of Arizona.

j. Where tangible personal property is to be acquired after the date hereof, that a security interest is created under the after-acquired property clause of the security agreement. [For use in a personal property secured loan transaction]

k. That the Note will be duly delivered for value and for the consideration provided for in or contemplated by the Documents and that value has been given for the creation of any security interest.

1. That the Company (and, where applicable, the guarantor) holds the requisite title and rights to any real or personal property involved in the Transaction or otherwise purported to be owned by it.

IV. Qualifications and Limitations

The opinions set forth above are subject to the following qualifications and limitations:

(1) The enforceability of the Documents may be subject to or limited by bankruptcy, insolvency, reorganization, arrangement, moratorium, and other similar laws relating to or affecting the rights of creditors generally;

(2) The enforceability of the Documents is subject to general principles of equity;

(3)(a) The enforceability of the Documents is subject to qualification that certain waivers, procedures, remedies, and other provisions of the Documents may be unenforceable under or limited by the law of the State of Arizona; however, such possible unenforceability or limitations will not render the Documents invalid as a whole or substantially prevent the practical realization of the principal benefits [or security] intended by the Documents (except for the economic consequences of procedural or other delay);

OR

(3)(b) The enforceability of the Documents is further subject to the qualification that certain waivers, procedures, remedies, and other provisions of the Documents may be unenforceable under or limited by the law of the State of Arizona; however, such law does not in our opinion, substantially prevent the practical realization of the benefits intended by the Documents [other than the guaranty] [except that the application of principles of guaranty and suretyship to the acts or omissions of the Lender after execution and delivery of the guaranty may prevent the practical realization of the benefits intended by the guaranty through a release or discharge of a guarantor].

(4) Our engagement did not extend to, and we render no opinion about, any federal or state [insert bodies of law—e.g. tax, securities, environmental, public health, or labor laws, rules or regulations, zoning matters, or applicable building codes or ordinances] or the effect of such matters, if any, on the opinions expressed herein.

(5) We express no opinion as to matters of title, priority, or perfection of liens or priority or perfection of security interests except as specifically set forth herein.

(6) Our opinion as to fixtures and personal property cover only (i) security interests created under Chapter 9 (Revised Article 9) of the Arizona

UCC, (ii) UCC collateral or transactions, and (iii) UCC perfection methods [that are limited to filing a financing statement].

(7) We are qualified to practice law in the State of Arizona, and we do not purport to be experts on, or to express any opinion concerning, any law other than the law of the State of Arizona and applicable federal law and, with respect to the opinions expressed in the _____ numbered paragraph above, solely the statutory provisions of the [corporate], [partnership], or [limited liability company] laws of the State of Delaware. Insofar as our opinion pertains to matters of _____ law, we have relied upon the opinion of Messrs. [firm name], of [city], [state] dated _____, a copy of which is attached. We do not purport to express any opinion concerning any law other than the law of the State of Arizona. [Although certain members of this firm are admitted to practice in other states, we have not examined the laws of any state other than the State of Arizona [and _____ and federal law] nor have we consulted with members of the firm who are admitted in other jurisdictions with respect to the laws of such jurisdictions.]

OR The Documents indicate that they are to be governed by the laws of the State of _____. We have no knowledge of those laws and express no opinion thereon. Irrespective of the law which is ultimately determined to apply to the Documents, however, if the Documents were governed by Arizona law, then our opinions set forth above would remain unchanged.

(8) The opinions expressed in this letter are based upon the law and facts in effect on the date hereof, and we assume no obligation to update, revise, or supplement this opinion.

(9) This opinion is being furnished to You solely for your benefit and may be relied on by You only for the purpose contemplated in the Transaction. Accordingly, it may not be: (i) used or relied upon by, or quoted or delivered to, any person or entity, or (ii) used or relied upon for any purpose other than the purpose contemplated in the Transaction without, in each instance, our prior written consent. [The primary opining lawyer may rely on the opinions set forth in paragraphs _____, _____ and _____ of this letter in rendering its opinion furnished pursuant to Section _____ of the _____ Agreement.]

(10) We express no opinion about the effect on the corporation or the Transaction, if any, of the provisions of A.R.S. section 43-1152 et seq.

(11) Although the opinions set forth in paragraphs 19 and 20 above are based upon an analysis of the assumed facts in light of the current applicable law, all as set forth above, we can give no assurance that a creditor or trustee of [the SPE] in a federal bankruptcy proceeding would

not attempt to have the assets and liabilities of [the SPE] substantively consolidated with those of an equity holder or Affiliate. Further, we express no opinion with respect to the availability of a preliminary injunction or other temporary relief pursuant to broad equitable powers granted to a federal bankruptcy court pending a final determination on the merits.

(12) We advise You that there are a number of inherent limitations in an opinion of this nature, including the pervasive equitable powers and discretionary judgment of the bankruptcy judge reviewing the facts and circumstances as they may exist at a future time, the overriding congressional goal of promoting reorganizations to which other legal rights and policies may be subordinated, the interplay of facts, circumstances, relationships and other considerations, some of which may not now exist, and the nature of the bankruptcy process. Further, an opinion is not a guarantee of what a court would hold; rather it is an informed judgment as to a specific question of law. Thus, this opinion is not a prediction of what a court would actually hold, but an opinion as to the decision a court would reach if the issue were properly presented to it and the court followed existing legal precedents applicable to the subject matter of this opinion.

Very truly yours,

[Law Firm] [Lawyer]

APPENDIX B

ILLUSTRATIVE OFFICER'S CERTIFICATE

The undersigned, hereby certifies to [LAW FIRM] ("Law Firm") for purposes of the opinion (the "Opinion") issued by Law Firm in connection with the [DESCRIPTION OF TRANSACTION] (the "Transaction"), that to the best of my knowledge and belief:

1. I, [NAME OF OFFICER], am the duly appointed, qualified and acting [OFFICER'S TITLE] of [ENTITY] (the "Company"). In my role as [TITLE] of the Company, I am responsible for [OFFICER'S DUTIES]. I am actively involved in the business operations of the Company and am generally familiar with [THE COMPANY'S CORPORATE AND BUSINESS AFFAIRS]. [DESCRIBE THE NATURE OF THE OFFICER'S DUTIES THAT DEMONSTRATE HIS/HER QUALIFICATIONS FOR MAKING THE CERTIFICATIONS]. I am familiar with the Transaction and the agreements, documents and instruments relating to the Transaction (the "Documents"). I [HAVE REVIEWED] [MAINTAIN AND HAVE CHARGE OF] the Company's minute book and all minutes and [CORPORATE] [COMPANY] records of the Company. All minutes of [BOARD OF DIRECTORS AND SHAREHOLDERS] [MEMBER(S)] [MANAGER(S)] [PARTNERS] were properly adopted [AT MEETINGS CALLED AND HELD AS REQUIRED BY THE [BYLAWS] [OPERATING AGREEMENT] [PARTNERSHIP AGREEMENT], AT WHICH A QUORUM WAS PRESENT AND FOR WHICH PROPER NOTICE WAS GIVEN] [PURSUANT A DOCUMENT EVIDENCING THE CONSENT OR APPROVAL OF THE ACTION TAKEN BY ALL [DIRECTORS] [MEMBERS] [MANAGERS] [PARTNERS]]. I have made such further examination, inquiry or investigation as is in my opinion necessary to enable me to make the certifications in this certificate.

2. The Company is engaged in the business of [NATURE AND SCOPE OF THE BUSINESS OF THE COMPANY, I.E., WHETHER THE COMPANY IS PUBLICLY TRADED, REGULATED BY A STATE OR FEDERAL SECURITIES AGENCY, TAX EXEMPT, ETC.]. The Company is regulated by [REGULATORY AGENCIES WITH OVERSIGHT RESPONSIBILITIES].

3. The following persons currently constitute all of the [BOARD OF DIRECTORS] [MEMBERS] [MANAGERS] [PARTNERS] [GENERAL PARTNERS] of the Company:

4. The following persons are duly elected or appointed and qualified officers of the Company and hold the offices set forth opposite their respective names below:

<u>Name</u>	<u>Office</u>
—	—
—	—

5. The State of Arizona [ADD OTHER STATES] is/are the only state(s) in which the Company owns, leases, licenses, or uses property or assets, or conducts business that is material to the operations of the Company.

I have examined a draft of the proposed Opinion which the Law Firm intends to deliver in connection with the Transaction and I know of no factual information or matter which would render untrue or inaccurate in any way the legal conclusions in the Opinion. This Certificate may be relied upon by the Law Firm in its Opinion delivered in connection with the Transaction. All of the information contained in this Certificate is true, correct and complete on and as of the date hereof.

IN WITNESS WHEREOF, the undersigned has executed this Opinion Certificate as of the ____ day of _____, 20_____.

[NAME OF ENTITY]

By: _____
Name: _____
Title: _____

APPENDIX C**BIBLIOGRAPHY**

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