

**DUTIES, OBLIGATIONS AND POTENTIAL
LIABILITY FOR SIGNING LEGAL OPINION LETTERS:**

Are You a Lawyer or a Gambler?

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“When a lawyer delivers a third-party closing opinion, she is placing herself in harm’s way to a greater extent than in perhaps any other aspect of business law practice.”¹

DUTIES, OBLIGATIONS AND POTENTIAL LIABILITY FOR SIGNING LEGAL OPINION LETTERS: Are You a Lawyer or a Gambler?

Introduction

The focus of this paper will be on “closing opinions”, sometimes known as “third party opinions”.² With some risk of oversimplification, opinion letters are prepared by an attorney for one party and presented to third parties, or the parties on the “other side” of a transaction, for their reliance. See Thomas L. Ambro and Arthur Norman Field, *The Legal Opinion Risk Seminar Papers*, 62 BUS. LAW. 397, 397 (2007). As a result, the attorney called on to provide an opinion letter ultimately provides advice to parties on both sides of the transaction. There are few reported decisions that offer guidance on this topic, and the majority of the literature and guidance has been developed by the American Bar Association and state bar associations. Its importance to municipal lawyers is great, as a request to provide a legal opinion to a non-client has become routine, and a regular part of the practice of municipal law.

Third party legal opinions date back to the 1800’s. Donald W. Glazer and Jonathon C. Lipson, *Courting the Suicide King: Closing Opinions and Lawyer Liability*, 17 BUS. LAW TODAY, Number 4 (March/April 2008). In those days, the railroad bond underwriters hired lawyers to provide legal opinions regarding the bonds, with such opinions actually printed on the bonds themselves. *Id.* Today, these opinions can have the effect of guaranteeing the accurateness and completeness of a transaction, seemingly replacing the due diligence of the

¹ Jonathan C. Lipson, *Price, Path & Pride: Third-party Closing Opinion Practice Among U.S. Lawyers (A Preliminary Investigation)*, 3 BERKELEY BUS. L.J. 59, 124 (2005).

² This paper is not a comprehensive review of all types of closing opinions. Instead, it is an outline of thoughts and questions for a municipal lawyer to consider when asked to provide a third-party opinion.

opinion recipient. See Koley Jensen, P.C., *Third-Party Legal Opinions: an Introduction to "Customary Practice"*, 35 CRLR 153, 154. This is especially scary for a municipal lawyer who shows up to a Council meeting to a stack of contracts, each tabbed for his signature at the bottom of a pre-drafted opinion letter.

As with many areas of law practice, the drafting of third-party closing opinions is fraught with potential traps for the unwary. One writer described the problem with closing opinion practice as follows:

The knowledge that someone is struck by lightning every year does not keep golfers off the golf course. Although the consequences are dire, the perceived risk is too small. Similarly, the knowledge that lawyers are now sued on opinions and that the damages sought can be catastrophic has not kept lawyers who work on financial transactions from giving third-party legal opinions. Lawyers see the risk to their careers of not giving opinions as large and the risk that they might be held liable for a substantial amount as small. Thus, they accept the risk of liability as going with the territory. Like golfers setting out on a rainy day, however, lawyers would do well to take what measures they can to protect themselves from the elements when they are proceeding, as they are now, under increasingly threatening skies.

*See Glazer and Lipson, *Courting the Suicide King*.*

Lawyers providing legal opinions are subject to many duties. A lawyer who fails to meet his ethical obligations may be subject to disciplinary proceedings; a lawyer who fails to meet the duty of care to his client may be liable for malpractice. See Charles E. McCallum and Bruce C. Young, *Ethics Issues in Opinion Practice*, 62 BUS. LAW. 417, 417 (2007). While there are no statistics related to third party opinion liability, the trend shows that claims based on closing opinions are on the rise. *Id.* Further, such claims can be the basis for criminal charges as well. As discussed later in this paper, it is clear that attorneys in some jurisdictions can be liable for

damages if they fail to exercise the skill and care ordinarily possessed by lawyers acting in similar circumstances. *See* McCallum and Young, at p. 418.

The role of an attorney in preparing information for the use of a third person does not fit into the “normal” attorney-client privilege. A lawyer undertaking such role “must be satisfied as a matter of professional judgment that making the evaluation is compatible with other functions undertaken on behalf of the client.” Tex. Disciplinary R. Prof’l Conduct 2.02, Comment 5. A lawyer has the duty to advise the client of the implications of potential results of the evaluation, particularly the attorney’s responsibilities to third persons and the duty to disseminate findings. *Id.* Importantly, the third party to whom the opinion is rendered does not develop an attorney-client relationship with the lawyer providing the opinion, but such attorney owes a duty to the third party to use care when the actual client has invited the third party to rely on their lawyer’s evaluation. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 51(2) (2000).

Texas lawyers are also guided by Texas Disciplinary Rule 4.01; Truthfulness and Statements to Others:

In the course of representing a client a lawyer shall not knowingly:
a) make a false statement of material fact or law to a third person;
or b) fail to disclose a material fact to a third person when disclosure is necessary to avoid making the lawyer a party a criminal act or knowingly assisting a fraudulent act perpetrated by a client.

Tex. Disciplinary R. Prof’l Conduct 4.01. The stakes are high, and attorneys must treat third-party opinions with the respect they deserve and require.

The Traps

The potential traps to be examined in this section are as follows: (1) possible liability through litigation; (2) confidentiality; (3) knowledge; (4) your client; and (5) particulars of actual drafting.

Possible Liability through Litigation

For his 2006 article entitled *Price, Path & Pride: Third-party Closing Opinion Practice Among U.S. Lawyers (A Preliminary Investigation)*, Professor Jonathan C. Lipson interviewed twenty-seven lawyers, the majority of whom had active involvement in third-party closing opinions. *Price, Path & Pride*, at p. 127. A common theme throughout Professor Lipson's interviews is the concern drafting attorneys have of possible liability through litigation. Admittedly, the facts and trends still make this a relatively small possibility, but one that appears to be growing. In fact, “[m]any of the lawyers interviewed for this project said that they thought that lawyers were becoming increasingly attractive litigation targets when transactions failed, and that opinion letters would form an important link in the chain leading to liability.” *Price, Path & Pride*, at p. 65.

This increasing attractiveness seems to be a result of many forces, including and possibly especially, the *Enron* scandal. This scandal, which came to light in October 2001, eventually led to the bankruptcy of the Enron Corporation, a Houston, Texas based energy company. At the time of its dissolution, Enron was the largest bankruptcy reorganization in American history and also the biggest audit failure. As reported in the Final Report of Neal Batson, the Court-Appointed Examiner of Enron, multiple law firms provided numerous closing opinions regarding “the ‘true sale’ of assets or the ‘true issuance’ of securities in complex and questionable transactions. According to the Examiner, in certain cases these opinions may have been inappropriate.” *Price, Path & Pride*, at p. 84; citing *Enron Final Report*, at p. 50 (internal citations omitted). Whereas these opinions were produced for Enron affiliates or the company itself, they were not technically “third-party” closing opinions. However, it seems that they were relied on by Enron’s accounting firm and certainly did not accomplish the goal of providing

accurate information. As Professor Lipson summarized, “it would appear that, whatever else may be true of Enron, closing opinions issued in certain of its transactions failed to perform their informational functions.” *Price, Path & Pride*, at p. 85. Finally, “it would appear that... Enron has generated a significant amount of anxiety about closing opinion practice.” *Price, Path & Pride*, at p. 107.

While there have been only few cases that have found attorneys liable for their involvement with third-party opinion letters, the perception seems to be that this result is increasing in regularity. As reported in Professor Lipson’s article:

[O]ne attorney from a mid-sized West Coast firm observed: “[T]he fact that there aren’t a lot of cases to hold lawyers liable and there isn’t a lot of experience of lawyers being sued, doesn’t mean that people aren’t fearful of it nevertheless. It’s like fastening your seatbelt on an airplane. I don’t know anyone who’s been through a plane crash, much less someone who has been through a crash who would not have survived if they weren’t wearing their seatbelt. Nevertheless, I buckle my belt low and firm across the lap.”

Price, Path & Pride, at p. 105. When drafting third-party opinion letters, attorneys should remember that perhaps the largest or most dangerous trap to avoid is liability through litigation.³

Breach of Confidential Information

Another potential trap to avoid is the breach of confidential client information. Clients entrust their attorneys with vital information that should not be compromised. One of the Guidelines for the Preparation of Closing Opinions, adopted by the Section of the Business Law of the American Bar Association in 2001, deals directly with this issue. Rule 2.4, entitled Client Consent and Confidential Information, states:

³ A later section of this paper will discuss litigation as a potential cost of providing opinion letters.

When the client's consent to the delivery of a closing opinion is required by applicable rules of professional conduct, that consent normally may be inferred from a provision in the agreement that makes delivery of a closing opinion a condition to closing. The opinions contained in a closing opinion ordinarily do not disclose information the client would wish to keep confidential. If, however, an opinion would require disclosure of information that the lawyers preparing the opinion are aware the client would wish to keep confidential, the implications should be discussed with the client and the opinion should not be rendered unless the client consents to the disclosure.

The Committee on Legal Opinions, *Guidelines for the Preparation of Closing Opinions*, 57 Bus. LAW. 875, 877-78 (2002).

In preparing third-party closing opinion letters, counsel should be aware of what information the client wants to keep confidential and what information it is allowable to disclose to the other party. Attorneys should also be aware of whether such possibility interferes with their ability to provide a reliable opinion to the third-party as called for in the terms of the transaction.

Knowledge

Any opinion is only as good as the information that led to the conclusion. If the attorney drafting the closing letter does not have good information, it will be impossible to provide a valid, reliable third-party closing letter. In fact:

One of the maxims of legal opinions is that they are only as good as the factual information upon which the opining lawyer has relied in rendering the legal opinion. The opining lawyer's job of gathering the information necessary to render the legal opinion usually is simplified by the fact that a large part of the transactional due diligence can also be used for the legal opinion. As a practical matter, the legal opinion due diligence is subsumed in the transactional due diligence.

Karen S. Rieger and Eric S. Fisher, *Maneuvering the Mundane Minefield: A Practical Guide to Legal Opinions in Healthcare Transactions*, 32 JOURNAL OF HEALTH LAW 173 (1999). In other

words, it is vital for the opining lawyer to have correct and accurate information. If inaccurate, incomplete or incorrect information provides the basis for a legal opinion, then the drafting attorney should be wary of providing such opinions.

Another related problem is when the actual drafting attorney does not have direct knowledge of particular information and has to rely on information provided by others. This situation is prevalent for municipal lawyers who are asked to provide opinion letters. This potential problem is in play when issuing a “no-violations” opinion.⁴ Professor Lipson stated, “[p]roblems with no-violations opinions may stem at least in part from the factual nature of the opinion. Unlike the due authority opinion, which is often based on the attorney’s first-hand knowledge of corporate governance actions leading to the transaction, the no-violations opinion might require the lawyer to investigate other transactions, other laws, or general states of affairs with which she has no direct experience.” *Price, Path & Pride*, at p. 78. Furthermore, “[m]ost of the lawyers interviewed for this project indicated that they had seen transactions change or even fall apart due to information produced in the process of negotiation and opinion drafting, and this was especially true of the no-violations opinion.” *Price, Path & Pride*, at p. 79. The diligent gathering and examination of such information is an important purpose of opinion letters, especially a “no-violations” letter.

Another “knowledge” trap for the unwary involves the situation where a lawyer is asked to provide an enforceability opinion. This type of opinion deals with documents written by opposing counsel, which could be a relative mystery to the drafting lawyer. This is one unique aspect of the American system regarding opinion letters. One attorney interviewed for Professor Lipson’s article pointedly opined that the enforceability opinion is “the toughest opinion to give

⁴ A “no-violations” opinion letter assures the recipient that the transaction is not a violation of any applicable organizational document, contract or law.

and often the toughest one that I've ever thought to justify ...because in essence what you're asking is for the lawyer for the borrower or the lawyer for the seller or whatever to say that the documents prepared by the lender's lawyer is or isn't enforceable." *Price, Path & Pride*, at p. 89, n. 151. Such an opinion could estopp the opinion givers client from later arguing certain positions in a subsequent lawsuit.

The quality of an evaluation depends on the freedom and extent of the investigation upon which it is based. Ordinarily a lawyer should have whatever latitude of investigation seems necessary as a matter of professional judgment. Under some circumstances, however, the terms of the evaluation may be limited. Tex. Disciplinary R. Prof'l Conduct 1.02. For example, certain issues or sources may be categorically excluded, or the scope of search may be limited by time constraints or the non-cooperation of persons having relevant information. Any such limitations which are material to the evaluation should be described in the report. If after a lawyer has commenced an evaluation, the client refused to comply with the terms upon which it was understood the evaluation was to have been made, the lawyer's obligations are determined by law, having reference to the terms of the client's agreement and the surrounding circumstances. Tex. Disciplinary R. Prof'l Conduct 2.02, Comment 6.

Your Client

While having your own client as a potential trap is something all attorneys would like not to worry about, it is nevertheless something that attorneys must be careful. First, as with all transactions or relationships, an attorney must truly know his or her clients. Succinctly put, "the fact that you have a reputable lawyer representing the client is no evidence of the client's honesty." *Price, Path & Pride*, at p. 86. The honesty of your client, or lack thereof, is

something which attorneys need to be aware. In fact, dishonesty or client fraud is a significant trap to which attorneys involved in this practice area must endeavor to avoid.

Not only should the opining lawyer be aware of the honesty and reputation of the client, the lawyer should also be aware of the overall health of the client. Due to the ever-changing and complex economic circumstances our country is currently facing, a looming problem for attorneys engaged in third-party opinion letter practice is that after giving an opinion, the client could fail to appropriate sufficient funds to finance the obligations upon which the lawyer opined.

Particulars of Actual Drafting

Of course there are numerous challenges and potential traps when the time to put pen to paper arrives. The most significant ones, in this author's opinion, will be outlined herein. First, clearly define the scope of the opinion. "To decrease the risk of liability for an opinion letter, opining counsel must carefully define the scope of the opinion and understand how the scope may change if the opinion adopts the [Legal Opinion] Accord."⁵ Lillian Blackshear, *Wait...What Did I Just Say?: What Lawyers Need to Be Concerned About When Issuing Third-Party Closing Opinions*, 10 THE TENNESSEE JOURNAL OF BUSINESS LAW 71, 75 (Fall 2008). It is easier to define the applicable scope of the opinion when the opinion adopts the standards of the Accord

⁵ An "Accord" opinion letter is one that has adopted the Legal Opinion Accord, which "is a collection of various assumptions, limitations, and interpretations that governs all opinions that adopt it. It was promulgated by the Business Law Section of the American Bar Association in 1991 as a way for opining counsel to standardize opinion letters and incorporate many of the customary assumptions and limitations in their opinions implicitly. Developed in response to the confusion that plagued opinion givers and recipients over the meaning of opinion provisions, the Accord is "a detailed set of rules that define[] for those who [choose] to adopt them how an opinion letter should be interpreted, the laws it should be understood to cover, the factual investigation the opinion giver [is] expected to conduct and the meaning of several standard opinion clauses." Blackshear, at p. 79 (internal citations omitted). While the Accord was drafted with the goal of bringing uniformity to opinion letter interpretation, its adoption into practice is uncommon. Blackshear, at n. 69.

A "Non-Accord" opinion letter is one that has not adopted the Legal Opinion Accord described above. "Non-Accord" opinion letters constitute the majority of closing opinion letters. Accordingly, counsel should be careful to clearly define the scope of the opinion letter.

because the Accord has adopted standards for different assumptions, limitations, and interpretations opinions. Blackshear, at p. 79. Otherwise, the drafting attorney should specifically define the scope of the opinion.

Second, when dealing with law that is unclear or subject to change, the drafting attorney should state precisely and directly that fact in the opinion. Blackshear, at p. 82. The lawyer should also communicate this fact to the client in other correspondence to further protect himself from potential liability. Blackshear, at p. 82. Of course, because lawyers are not expected to possess psychic qualities, they are not required to accurately predict the future state of the law.

According to the American Bar Association's Committee on Legal Opinions, both Accord and non-Accord opinion letters "speak[] as of [their] date. An opinion giver has no obligation to update an opinion letter for subsequent events or legal developments." Thus, the problem is not that the law is uncertain or likely to change; the real problem is how to issue such an opinion. As is often the case, honesty is the best policy." Blackshear, at p. 81. Attorneys should directly state in the opinion and other correspondence with the client that the law is unsettled or could change. That way, this potential trap will be minimized.

Next, it is important for the opinion drafters to clearly and unambiguously define key terms that may be subject to various interpretations. Succinctly put, "[w]hen the meaning of certain words or phrases is ambiguous, it is likely that different parties will interpret the words or phrases differently. When interpretations differ, litigation may follow." Blackshear, at p. 83. Terms such as "to our knowledge," "no litigation," "threat of litigation," and "material" are just a few examples that could be construed ambiguously and attorneys should consider having these terms specifically defined.

One last, yet important point to examine when drafting an opinion letter is to determine whether the opinion is to be issued by the law firm or only the attorneys drafting the letter. “[I]f an opinion letter is signed by a firm, the opinion is considered to be issued by the entire firm and not just the lawyers who participated in drafting the opinion. ‘To our knowledge’ in a firm-issued opinion means ‘to the knowledge of all the lawyers in this firm.’ If a firm represents a client in several different capacities, lawyers drafting the opinion letter for the client should verify with other lawyers working for the client that the opinion letter is accurate. ‘There is no absolute requirement that every lawyer be consulted and every file reviewed. Informal consultations will satisfy the due diligence inquiry, provided that the opinion preparer talks to the appropriate people.’” Blackshear, at p. 90 (internal citations omitted).

Cost-Benefit Analysis

Client-Recipient

One of the first things that should come to mind when a lawyer is requested to provide an opinion is the cost to their client and the benefit to the recipient. See Glazer and Lipson, *Courting the Suicide King*. The cost to a client centers on the legal expense of an attorney preparing the opinion, and the research and diligence required. Unfortunately, it can be difficult to determine the cost of an opinion before undertaking such task. The benefit to the recipient focuses on the assurance that any legal concerns they might have about the transaction have been reviewed and addressed by the opinion provider.

The initial analysis can and should include determining whether such an opinion would be overly expensive for the transaction contemplated or of little value to the recipients. For example, in a transaction involving an interest rate, the client should receive some benefit for providing the legal opinion. If the interest to be assessed and other material terms are the same

whether a legal opinion is provided or not, there can be little benefit to the client in providing the opinion. However, if there is one interest rate to be charged with the provision of a legal opinion, and a higher cost for the transaction without a legal opinion, a calculator can help assess whether the cost-benefit analysis favors the client.

***Attorney*⁶**

The second analysis is the cost-benefit analysis for his/her own work. Today, the risk of being sued on an opinion is real, and litigation-related costs must be considered if an attorney is going to make a proper analysis as to whether to issue an opinion and if so, how much should he charge. To be able to analyze the potential cost to an attorney, the attorney has to be able to identify the potential costs moving forward. One of the difficulties in making such an analysis is that such suits against attorneys are not likely to be resolved with a motion to dismiss. These actions are fact specific, and plaintiffs are generally given the opportunity to develop the facts.

No matter how professional attorneys may have been in preparing their opinions, law firms continue to be targets of potentially catastrophic suits. The question must be one that, given your practice, the opinions you give, and procedures you have in place, whether you have fully considered the risks you have been running when delivering third-party opinions. The challenge for lawyers engaging in third-party opinion practice, as with most any area of law, is to maximize the benefits while minimizing the costs. This must be done in the context of clients who are likely to question the significance of cost for a “simple letter.”

It has been suggested that legal opinions create at least four classes of costs for attorneys: Negotiation; Diligence; Legal Research; and Firm Process Costs (i.e. having the opinions committee vet the opinion).

⁶ This section relies heavily, or perhaps almost exclusively, on Jonathon Lipson’s 2008 article *Cost-Benefit Analysis and Third-Party Opinion Practice*.

1. Negotiation focuses on the time spent negotiating with attorneys for the opinion recipient as to what can and should be included in an opinion, and what ought to be excluded from an opinion. In a municipal practice, an attorney is often given a pre-printed form, included in a set of loan, financing or other contractual documents, and asked to sign. Many times, the attorney has been excluded from the contract negotiations, and knows little or nothing about the transaction details. However, clients often do not understand why an attorney feels compelled to negotiate the terms and breadth of an opinion – after all, the parties have usually already signed the preprinted contracts where instructed. Regardless, negotiation can and will be necessary, bringing with it costs to the client.

2. Diligence by the attorney also eats up valuable time and money. In order to provide a valid opinion, an attorney must review the applicable documents to ensure he or she is comfortable with the requirements of the opinion recipient. Diligence obviously increases with the complexity of any transaction.

3. Legal research lies at the heart of any legal opinion, whether drafted for the benefit of a client or third party. An opining attorney must review the law applicable to the underlying transaction. Depending on the transaction in question, extensive legal research might be necessary. More scary, the person asked to sign the opinion letter might not have the background, experience or knowledge to so opine.

4. Firm process costs can be easy to overlook. A responsible attorney will have any opinion letter vetted by the Firm's opinion committee. This committee should consist of multiple attorneys with the necessary skill set to assess the propriety of the opinion in addition to the potential risk to the Firm. In the days of plaintiffs seeking to attach significant liability to an opinion giver, the future of a Firm might well depend on the soundness of the opinion measured

against the Firm's risk. The costs of this review can be significant with the involvement of multiple attorneys.

More important than these "hard costs" may be the less obvious cost of potential liability. Liability for third-party opinions is a source of much debate. Traditionalists argue liability should not exist where there is no attorney-client privilege. However, recent examples from around the country illustrate that such concerns must be considered when evaluating risk.⁷

Finally, many attorneys attach a non-economic cost to this portion of their practice. For some, research reveals that opinion practice is more stressful and aggravating than other parts of their practice. Concerns about potential liability are often at the center of this stress. An attorney's potential damage to their reputation also plays into their fear. *Id.*

The Opinion Committee

Few of the reports, articles and treatises on legal opinions discuss the law firm practices to see that opinions are rendered in a proper manner. Committee on Legal Opinions, ABA Section of Business Law, *Law Office Opinion Practices*, 60 Bus. Law. 327 (2004). The ABA Section of Business Law, Committee on Legal Opinions, has recommended that law firms that deliver closing opinions should "periodically consider their policies and procedures for giving and receiving opinions and mirror changes in their practice and personnel with development in the law." *Id.* In a survey conducted by the ABA, it is apparent that there was wide variation in law firm instruction regarding opinion committees, explanatory materials provided to firm attorneys and the extent of formal education and written guidance on this subject. *Id.* at 328. Some, but not all, firms sought uniformity in their opinions.

⁷ Committee on Legal Opinions, ABA Section of Business Law, *Crossing the Threshold: Why Ask for an Opinion at All?* (2007), available at <http://apps.americanbar.org/buslaw/tribar/materials/20090715000003.pdf>.

Consultation with other lawyers in the firm should be a basic of the firm's culture. Many firms require consultation with at least one fellow attorney prior to giving an opinion. *Id.* at 329. Other firms that do not require consultation in basic or routine opinion matters might well require consultation where the project involves different legal or factual issues or involves a new client. *Id.* These intra-firm consultations can often be informal, or formalized where the firm has a mechanism for assigning a second lawyer to provide consultation. Legal malpractice insurance carriers are often now encouraging or requiring the use of some kind of formal consultation system. *Id.* at 330. Of course, such a consultant system assumes that the required expertise is available at the opinion giver's firm. If not, experts outside the firm should be consulted, either formally or informally. *Id.*

One of the functions of opinion committees is education. While they may also serve as a basis for formal or informal consultation, providing education from internal and external sources can be beneficial. In more formal opinion committees, there are prepared forms, policy statements and opinion manuals. These committees should also address the issue of limits on a firm's willingness to give opinions. Such a committee can also serve as a central base to maintain files of previous opinions, as well as make a post-opinion determination on whether internal policies were followed.

While there is no universally accepted model or requirement for a consultation or an opinion committee, the foundational concept that two or more heads are better than one can serve to provide the opinion giver better assurance that his opinion is proper and sustainable. It also provides protection for the firm from potential catastrophic losses as a result of the opinion.