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# Legal Opinions in Corporate Transactions: The Opinion on Agreements and Instruments

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Legal Opinions in Corporate Transactions: The Opinion on Agreements and Instruments

Scott FitzGibbon\* and Donald W. Glazer\*\*

I. INTRODUCTION . . . . . 657
II. WHAT THE OPINIONS MEAN . . . . . 660
A. "Duly Authorized, Executed and Delivered" . . . . . 660
1. Duly Authorized . . . . . 660
2. Duly Executed . . . . . 665
3. Duly Delivered . . . . . 666
B. "Legal, Valid and Binding" . . . . . 667
C. "Enforceable in Accordance with its Terms" Subject to the Equitable Principles Qualification . . . . . 686
D. The Bankruptcy Qualification . . . . . 689
III. GIVING THE OPINION . . . . . 693
A. Supporting the Opinion . . . . . 693
B. Handling Defects . . . . . 695

I. INTRODUCTION

When a lawyer delivers a legal opinion in a corporate transaction he confirms that the transaction is what it is meant to be from a legal point of view. Central

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First session: Robert Nutt and Philip Smith of Ropes & Gray.

Second session: Truman Casner of Ropes & Gray; David Herwitz, Austin Wakeman Scott Professor of Law, Harvard Law School; and Kenneth Novack of Mintz, Levin, Cohn, Ferris, Glovsky and Popeo.

Third session: Stephen Case of Davis Polk & Wardwell; E. Allen Farnsworth, Alfred McCormack Professor of Law, Columbia University; Arthur Field of Shearman & Sterling; James Fuld of Proskauer, Rose, Goetz & Mendelsohn; and Charles Hoppin of Davis Polk & Wardwell.

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to such an opinion is the paragraph that passes on the agreement and certain related instruments: for example, the stock purchase and sale contract or underwriting agreement in an equity financing, the merger agreement in a reorganization, or the loan agreement and notes in a bank financing. The opinion typically states that the agreement is "duly authorized, executed and delivered by the Company and is a legal, valid and binding obligation of the Company and is enforceable against the Company in accordance with its terms,"<sup>1</sup> subject to "bankruptcy" and "equitable principles" qualifications along the following lines:

[e]xcept as may be limited by bankruptcy, insolvency or other similar laws affecting the enforcement of creditors' rights in general. The enforceability of the Corporation's obligations under the Agreement is subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).<sup>2</sup>

Lawyers sometimes omit portions of the standard formula, but they rarely substitute new phrases:

Although the words of the opinion on agreements and instruments are fixed,

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1. Another formulation of the duly authorized, executed and delivered opinion is as follows: "The execution, delivery and performance of the Agreement, including the issuance and delivery of the Shares and the Note, have been duly authorized by all requisite corporate action, and the Agreement and the Note have been duly executed and delivered by the Corporation." Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyers' Association, *Legal Opinions to Third Parties: An Easier Path*, 34 BUS. LAWYER 1891, 1912-14 (1979) [hereinafter *New York Report*].

When the obligations to which the opinion relates are those of an individual rather than a corporation, the term "authorized" is sometimes omitted. Under those circumstances, the opinion sometimes states that the individual had the requisite capacity to enter into, execute, and deliver the agreement or instrument.

In an offering of securities registered under the Securities Act of 1933, registrants are required to file with the Securities and Exchange Commission "[a]n opinion of counsel as to . . . whether . . . debt securities . . . will be binding obligations of the registrant." Item 601(b)(5)(i) of Regulation S-K, 17 C.F.R. § 229.601(b)(5)(i) (1986), 6 Fed. Sec. L. Rep. (CCH) ¶ 71,071.

2. *New York Report*, *supra* note 1, at 1914. The "bankruptcy" and "equitable principles" qualifications make take various other forms. See *infra* text accompanying notes 101-11.

The "equitable principles" qualification often is drafted to modify only the "enforceable in accordance with its terms" opinion. There may be benefits, however, in drafting it to modify "legal, valid and binding" as well. See *infra* text accompanying note 110.

their meanings are surprisingly unsettled. The standard phraseology, replete with fuzzy nouns and slippery adverbs, is susceptible to a broad range of interpretations. This Article describes the various meanings that have been attributed to each phrase<sup>3</sup> and recommends standard interpretations.<sup>4</sup>

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3. As set forth in the second asterisk footnote above, this Article attempts to take into account the views of a great many experienced corporate lawyers who deliver opinions regularly in major corporate transactions. Most of those lawyers never have taken the time to commit their views to writing.

This Article also reflects the views expressed at professional conferences and in published commentaries. Important works on legal opinions include: A. JACOBS, *OPINION LETTERS IN SECURITIES MATTERS: TEXT—CLAUSES—LAW* (1987 rev. ed.); *LEGAL OPINIONS AND ACCOUNTANT CERTIFICATIONS* (Practicing Law Institute 1975); *OPINION LETTERS AND RECENT DEVELOPMENTS: FOURTH ANNUAL CORPORATE AND SECURITIES LAW CONFERENCE* (Massachusetts Continuing Legal Education, Inc., 1986); *OPINION LETTERS OF COUNSEL 1985* (Practicing Law Institute 1985); *OPINION LETTERS OF COUNSEL 1984* (Practicing Law Institute 1984); Komaroff, *What is a Clean Opinion Like You Doing in a Situation Like This?*, in 1 *RESOURCE MATERIALS: BANKING AND COMMERCIAL LENDING LAW* 501 (ALI-ABA 1980); Ryan, *Legal Opinions to Third Parties, Representations, and Warranties Covering Security Interests in Personal Property*, in 2 *RESOURCE MATERIALS: BANKING AND COMMERCIAL LENDING LAW* 121 (ALI-ABA 1981); Babb, Barnes, Gordon & Kjellenberg, *Legal Opinions to Third Parties in Corporate Transactions*, 32 *BUS. LAW.* 553 (1977); Bermant, *The Role of the Opinion of Counsel: A Tentative Reevaluation*, 49 *CAL. ST. B.J.* 132 (1974); Committee on Opinions, National Association of Bond Lawyers, *Model Bond Opinion Project*, 15 *URB. LAW.* 985 (1983); FitzGibbon & 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 (1986); FitzGibbon & Glazer, *Legal Opinions on Incorporation, Good Standing, and Qualification to Do Business*, 41 *BUS. LAW.* 461 (1986) [hereinafter FitzGibbon & Glazer, *Legal Opinions on Incorporation*]; FitzGibbon & Glazer, *Legal Opinions on Secondary Sales of Stock*, 30 *BOSTON B.J. NOV.-DEC.* 1986, at 30; Fuld, *Lawyers' Standards and Responsibilities in Rendering Opinions*, 33 *BUS. LAW.* 1295 (1978) [hereinafter Fuld II]; Fuld, *Legal Opinions in Business Transactions—An Attempt to Bring Some Order Out of Some Chaos*, 28 *BUS. LAW.* 915 (1973) [hereinafter Fuld I]; Harter & Klee, *The Impact of the New Bankruptcy Code on the "Bankruptcy Out" in Legal Opinions*, 48 *FORDHAM L. REV.* 277 (1979); Boston Bar Association Securities Law Committee, *Report by Boston Bar Association Securities Law Committee on Securities Law Opinions in Exempt Offerings*, 30 *BOSTON BAR J.*, NOV.-DEC. 1986, at 6; *Report of the Committee on Corporations Regarding Legal Opinions in Business Transactions*, 14 *PAC. L.J.* 1001 (1983) [hereinafter *California Report*]; Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyers' Association, *An Addendum—Legal Opinions to Third Parties; An Easier Path*, 36 *BUS. LAW.* 429 (1981); Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyers Association, *Legal Opinions to Third Parties: An Easier Path*, 34 *BUS. LAW.* 1891 (1979); Subcommittee on Opinion Writing of the Massachusetts Bar Association, Committee on Corporate, Banking and Business Law, *Omnibus Opinion for Use by Seller's Counsel in the Sale of a Closely-Held Business*, 61 *MASS. L.Q.* 108 (1976) [hereinafter *Massachusetts Sale of Closely-Held Business Report*]; Subcommittee on Opinion Writing of the Massachusetts Bar Association, Committee on Corporate, Banking and Business Law, *Omnibus Opinion for Use in Loan Transactions*, 60 *MASS. L.Q.* 193 (1975) [hereinafter *Massachusetts Loan Transactions Report*]; Business and Corporations Law Section, Los Angeles County Bar Association, *Legal Opinions in Business Transactions* (Dec. 8, 1983); California Continuing Education of the Bar, *Problems and Pitfalls in Preparing and Issuing Attorney's Opinion Letters* (1976); Case & Bernstein, *Effect of the Bankruptcy Reform Act of 1978 on Opinions of Counsel in Investment and Other Transactions* (Mar. 22, 1980); Committee on Developments in Business Financing of the Section of Corporation, Banking and Business Law, American Bar Association, *TERM LOAN HANDBOOK* (1983) [hereinafter *TERM LOAN HANDBOOK*].

4. The authors of this Article, a law professor and a practicing lawyer, are writing a book on legal opinions in corporate transactions of which this Article will be a part. The book, entitled *LEGAL OPINIONS IN CORPORATE TRANSACTIONS*, is to be published by Little, Brown and Company.

## I. WHAT THE OPINION MEANS

## A. "Duly Authorized, Executed and Delivered"

The phrase "duly authorized, executed and delivered" appears in virtually all opinions. It means that at the time of entering into the agreement or creating the instrument, the corporation had the corporate power and was permitted under corporate law and by its charter and by-laws, to enter into the agreement or to create the instrument and to perform its obligations. The phrase also means that the agreement or instrument and the performance by the company of its obligations have been approved to the extent required by the stockholders, directors, or officers of the corporation; that the agreement or instrument has been signed on behalf of the corporation by persons who had the power to do so; and that it has been delivered in such a manner as to bring it into effect. As so defined, the phrase focuses on the creation of the agreement or instrument, rather than on remedies for its breach. Lawyers rarely have any real problem opining that an agreement or instrument has been "duly authorized, executed and delivered."

1. *Duly Authorized*

The opinion that an agreement or instrument is "duly authorized" has both substantive and procedural aspects. First, the "duly authorized" opinion confirms that the company was a corporation at the time action was taken to authorize the agreement or instrument. Thus, the lawyer could not give the "duly authorized, executed and delivered" opinion about an asset purchase agreement entered into by a promoter purporting to act on behalf of the company prior to its incorporation unless the agreement was approved by the corporation after it was organized.<sup>5</sup> Similarly, the lawyer could not give the opinion if the agreement or instrument was authorized after the corporation had been dissolved or after its charter had been suspended.<sup>6</sup>

Second, the "duly authorized" opinion confirms that under corporate law and the company's charter and by-laws, the company had the power to enter into the agreement or to create the instrument and to perform its obligations. The opinion could not be given, for example, about a joint venture partnership agreement when corporate law or the company's charter denied it the power to be a partner,<sup>7</sup> nor could it be given about a pledge or guaranty given to support a parent company's borrowings that was ultra vires because it did not further

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5. For a description of the theories under which a corporation may, by some action on its part, become liable on a preincorporation contract, see H. HENN & J. ALEXANDER, *LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES* § 111 (3d ed. 1983).

6. Under the law of some states, the agreement would be validated once the corporation is revived. Massachusetts law provides, "Upon the filing of a certificate reviving a corporation for all purposes . . . all acts and proceedings of its officers, directors and stockholders . . . which would have been legal and valid but for such dissolution, shall . . . stand ratified and confirmed." MASS. GEN. L. ch. 156B, § 108 (1984). For a case indicating that agreements entered into by the corporation after it has been involuntarily dissolved become enforceable once the corporation is reinstated, see *Regal Package Liquor, Inc. v. J.R.D., Inc.*, 125 Ill. App. 3d 689, 693, 466 N.E.2d 409, 412 (1984).

7. The Massachusetts statute denies a corporation that power unless its charter expressly provides for it. See MASS. GEN. L. ch. 156B, § 9A (1984).

the corporate purposes of the subsidiary.<sup>8</sup> Similarly, the opinion could not be given about a debt instrument that contravened a borrowing restriction in the portion of the charter establishing a class of preferred stock. In *Chemical Bank v. Washington Public Power Supply System*, financing arrangements were struck down as ultra vires because of lack of statutory power on the part of municipalities and other governmental units.<sup>9</sup>

Third, the "duly authorized" opinion confirms that the proper corporate body has approved the agreement or instrument in the manner required by corporate law, the charter, and the by-laws.<sup>10</sup> As *General Overseas Films, Ltd. v. Robin International, Inc.* illustrates, a lawyer could not opine that a guaranty of a substantial obligation of another company, for example, was "duly authorized" when it was not approved by the board of directors of the guarantor.<sup>11</sup>

Statutes, charters, and by-laws usually require director or shareholder approval for specified matters but provide little guidance with respect to what approvals are needed for other matters. Most states have little case law on the point.<sup>12</sup>

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8. The Delaware statute recently was amended to authorize guaranties of affiliate obligations under certain circumstances. See DEL. CODE ANN. tit. 8, § 122(13) (Supp. 1986).

Guaranties of the obligations of affiliates raise several other legal questions. Courts sometimes construe guaranties narrowly and are generous in allowing contract law defenses to guarantors. See Alces, *The Efficacy of Guaranty Contracts in Sophisticated Commercial Transactions*, 61 N.C.L. REV. 655 (1983). Guaranties sometimes are subject to attack as fraudulent conveyances. See *infra* notes 114-23 and accompanying text. Guaranties may violate management's fiduciary duties or, when they support a shareholder's obligations, may constitute an unlawful dividend or distribution to the shareholder. In a bankruptcy proceeding, guaranties may be subjected to equitable subordination or, under some circumstances, be avoided if made within a year of bankruptcy. See § 548(a) of the Bankruptcy Code, 11 U.S.C. § 548(a) (1982). Valuable works on the legal problems of guaranties include: P. BLUMBERG, *THE LAW OF CORPORATE GROUPS: PROBLEMS IN THE BANKRUPTCY OR REORGANIZATION OF PARENT AND SUBSIDIARY CORPORATIONS, INCLUDING THE LAW OF CORPORATE GUARANTIES* (1985); Schneider, *Opinions on Guarantees, Leveraged Buyouts and Secured Transactions*, in *OPINION LETTERS AND RECENT DEVELOPMENTS* 327 (Massachusetts Continuing Legal Education 1986); Clark, *The Duties of the Corporate Debtor to its Creditors*, 90 HARV. L. REV. 505 (1977). For a brief discussion of how lawyers cure legal problems raised by guaranties, see *infra* text accompanying notes 131-33.

9. 99 Wash. 2d 772, 798, 666 P.2d 329, 342 (1983), *aff'd on remand*, 102 Wash. 2d 874, 691 P.2d 524, *cert. denied*, 471 U.S. 1065 (1985).

10. One commentator has recommended the use of the phrase "duly authorized by all necessary corporate action on the part of the Company" rather than simply "duly authorized" in order to "negate the implication that the opinion includes authorization other than as required under corporate law (e.g., by a governmental regulatory body or another third party whose consent may be required)." Halloran, *Rendering Opinions of Law—Opinions in Registered Offerings*, in *OPINION LETTERS OF COUNSEL*, *supra* note 3, at 9, 22-23 (discussing the opinion of issuer's counsel as to the due authorization of the underwriting agreement in a public offering); *accord California Report*, *supra* note 3, at 1036. The term "by the Company," without more, would appear to be sufficient to rule out any implication that the opinion covers approvals by anyone else.

In some jurisdictions the presence of the corporate seal on an instrument constitutes prima facie evidence that execution of the instrument was authorized by the corporation. See, e.g., N.Y. BUS. CORP. LAW § 107 (McKinney 1986).

11. 542 F. Supp. 684 (S.D.N.Y. 1982), *aff'd*, 718 F.2d 1085 (2d Cir. 1983). The court indicated that a corporate treasurer had neither actual nor apparent authority to give the guaranty. *Id.* at 691-92.

12. For a good discussion of the limits on delegation of board authority, see *Boston Athletic Ass'n. v. International Marathons, Inc.*, 392 Mass. 356, 363, 467 N.E.2d 58, 62 (1984) (holding that the board lacked power to "delegate authority which is so broad that it enables the officer to bind the corporation to extraordinary commitments or significantly to encumber the principal asset or function of the corporation.").

As a matter of good practice, corporations typically obtain director approval of matters important enough to call for an opinion of counsel whether or not the law requires it. When shareholder or director approval is not required and is not obtained, the lawyer must determine whether the agreement or instrument was authorized by the proper officers.<sup>13</sup>

Corporate law requires some agreements to be approved by the directors before they are executed and by the shareholders before they are performed. Examples of this sort of agreement are merger agreements and agreements relating to the sale of corporate stock in excess of the amount previously authorized. When shareholder approval is not stated in the agreement to be a condition to performance, the opinion should not be given without an express qualification pointing out that further approvals are needed. A harder case is presented where the agreement by its terms makes shareholder approval a condition of the company's obligations. Under those circumstances it might be argued that the agreement has been duly authorized even though performance requires shareholder action. In the recent case of *ConAgra, Inc. v. Cargill, Inc.*, however, the Nebraska Supreme Court adopted the view that a requirement of shareholder approval is more than a condition of the company's obligation and that no contract can be formed until it is obtained.<sup>14</sup>

The "duly authorized" opinion does not mean that the directors, in approving the agreement or instrument, were in compliance with their fiduciary duties. Fiduciary questions are largely factual in nature and turn on the purposes and intentions of the directors and the fairness of the transaction. An assumption

The smaller the corporation and the larger the transaction, the more likely that director approval will be required. In very large corporations officers—even divisional officers—often have authority to commit the corporation to transactions that for small companies would require board approval.

13. See *infra* text accompanying notes 22-23.

14. 222 Neb. 136, 382 N.W.2d 576 (1986). ConAGRA and MBPXL had entered into a merger agreement including a clause that stated:

*Best Efforts.* The respective Boards of Directors and principal officers of each of ConAGRA and MBPXL shall take all such further action as may be necessary or appropriate in order to effectuate the transactions contemplated hereby including recommending to their respective shareholders that the merger be approved; *provided, however,* nothing herein contained shall relieve either Board of Directors of their continuing duties to their respective shareholders.

222 Neb. at 146-47, 382 N.W.2d at 582. See generally Note, *Target Directors' Fiduciary Duty Overrides Contractual Duty in Merger Contracts*, 12 J. Corp. L. 735 (1987) (discussing the *ConAgra* directors' fiduciary duty stemming from the best efforts clause).

The MBPXL directors, however, later recommended that the shareholders accept an offer from Cargill, Inc. ConAGRA sued MBPXL and Cargill for violation of the agreement. The court concluded that ConAGRA was not entitled to recover. The court based its decision largely on the language in the agreement quoted above giving the directors a right to fulfill their duties to the shareholders. But the court also noted that:

[T]he directors could not enter into an agreement to violate their fiduciary obligations to their shareholders and then render the company and ultimately the shareholders liable for failing to carry out an agreement in violation of the directors' duty to the shareholders. To so hold, it would seem, would be to get the shareholders coming and going.

222 Neb. at 156, 282 N.W.2d at 587. The court also stated that "[s]everal courts have held that analogous agreements are without legal binding effect absent shareholder approval." 222 Neb. at 156, 182 N.W.2d at 588.

about compliance with fiduciary obligations is implicit in all opinions and ordinarily need not be spelled out. When fiduciary questions are particularly sensitive, however, lawyers often choose to state the assumption expressly. For example, some law firms as a matter of policy include a carefully drafted disclaimer whenever they pass on agreements for the sale of "crown jewels" and other agreements entered into as antitakeover devices since those transactions are often challenged on the grounds that they violate management's fiduciary duties.<sup>15</sup> Assumptions and disclaimers, however, no matter how carefully drafted, will not solve the problem when a lawyer believes that a transaction violates a board's fiduciary obligations, and a lawyer should decline to give the opinion on such a transaction.

Fourth, the "duly authorized" opinion confirms that director or shareholder action, if required, has been taken in compliance with procedural requirements. These requirements include not only the standard by-law provisions relating to the call and conduct of meetings, but also to special statutory requirements such as the rule in some states that interested transactions be approved by a majority of the disinterested directors or shareholders.<sup>16</sup> When a board committee has acted, the opinion also confirms that corporate law and the charter and by-laws permit committee action on the matter<sup>17</sup> and confirms that the committee acted within the scope of its authority.

Absent knowledge to the contrary, a lawyer can rely upon recitals in the minutes about the status of those acting as shareholders or directors and about procedural matters such as the giving of notice, the presence of a quorum, and the disclosure of any personal interest. Lawyers also often rely upon a secretary's certificate with respect to the incumbency of directors and officers and similar matters. When lawyers have concerns about the company's internal procedures, however, they sometimes go further and confirm through a corporate record check that where board action is required, the directors who approved the transaction were duly elected.

Fifth, the "duly authorized" opinion confirms that the agreement or instrument in question is the one approved by the directors or shareholders. Ordinarily, the resolutions adopted by the directors or shareholders refer to a specific agreement or instrument, approve it, and authorize the officers to execute it in the form presented to the meeting "with such changes therein as the officers executing the agreement may approve, their execution thereof to be conclusive evidence of their authority to do so." An elastic resolution of this sort permits the lawyer to give a "duly authorized" opinion even if the executed agreement differs substantially from the form presented to the meeting. However, officers are not free to make whatever changes they see fit: a board's power to delegate authority is not unlimited, and at some point changes may be so extensive that

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15. See, e.g., *Hanson Trust PLC v. ML SCM Acquisition, Inc.*, 781 F.2d 264 (2d Cir. 1986); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986). Similar questions may be presented when the company acquires assets as an antitakeover device. See *Royal Indus. v. Monogram Indus.*, [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,863 (C.D. Cal. Nov. 29, 1976) (enjoining, as a violation of management's fiduciary duties, an acquisition intended to create an antitrust barrier to a hostile tender offer).

16. E.g. ILL. ANN. STAT. ch. 32, ¶ 8.60 (Smith-Hurd 1985).

17. In many states committee action would not, for example, be sufficient to authorize a merger.



the company is, in effect, entering into an agreement entirely different from the one approved by the board. Thus, when major changes have been made, counsel must consider whether they are so fundamental, that further board action is required.<sup>18</sup>

In some cases, directors or shareholders approve an agreement or instrument in general terms only without referring to a specific draft or reciting more than the most basic provisions. In other cases, the resolutions do no more than approve a specified transaction and authorize the officers to execute such agreements and instruments as may be necessary or desirable in order to effect it. In all such cases where broad discretion has been conferred on the officers, the lawyer must determine whether shareholder or director approval was, in fact, required and, if so, whether the shareholders and directors did enough under applicable law to satisfy that requirement. Courts in modern times usually have permitted officers broad discretion in implementing directors' actions. How much discretion can be conferred on the officers will depend on the nature and size of the transaction, its significance to the corporation, the applicability of any statutory requirement for board approval, and the degree to which the agreement imposes restraints on future board action. The amount of discretion also may depend on which officers are authorized by the resolution to act on behalf of the corporation and the practice followed by the directors in previous transactions. Lawyers will find it easier to conclude that a general resolution is sufficient if it authorizes only the president and perhaps a few other top officers to execute the agreement and approve changes and if the terms of the agreement as executed are consistent with the term sheet or other description of the proposed agreement furnished to the directors prior to their vote. Depending on the circumstances, lawyers sometimes also insist that another meeting be held, perhaps by telephone conference call in the case of a directors' meeting, to authorize or ratify all the acts that have been taken and all the agreements that have been prepared since the original vote.<sup>19</sup>

Lawyers often prepare resolutions for adoption at the meeting. Sometimes, however, the shareholders or directors approve the transaction before resolutions have been drafted and leave it to the lawyer to prepare detailed resolutions after the meeting.<sup>20</sup> In some cases the minutes, including the detailed resolutions, are approved by the directors before the opinion is rendered. Where the opinion is given prior to such approval, lawyers usually have the secretary certify that the resolutions were duly adopted.

Sixth, when the instrument in question is a bond issued under an indenture or an option created under a stock option plan, the "duly authorized" opinion confirms that the indenture or plan has been "duly authorized" and that the instrument in question complies with its requirements. Indentures often (1) require trustee authentication and other procedures for the creation of new bonds; (2)

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18. The factors that counsel should consider are similar to those applicable when the board approves an agreement only in general terms.

19. Even when counsel can give an opinion on a transaction approved by the board in general terms only, the directors may be subject to liability if they have not discharged their duty of care. See *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985); see Note, *supra* note 14, at 755.

20. The lawyer should resist the temptation to draft resolutions that overstate what happened. For example, if the board approved a merger on the basis only of a term sheet or an oral description of the proposed transaction, the resolutions should not be drafted to state that the directors approved the merger agreement "in the form presented to the meeting."

specify the form of the bonds; and (3) state which offers are authorized to execute them.<sup>21</sup> Indentures often also prohibit the issuance of new bonds unless certain requirements, such as financial ratio tests, are satisfied. To confirm compliance with such requirements, lawyers generally rely on officers' certificates. Lawyers do not normally look behind such certificates to confirm the accuracy of the calculations, but they may find themselves called upon to interpret informally the meaning of certain financial tests.

## 2. *Duly Executed*

The opinion that an agreement or instrument has been "duly executed" means that it has been signed either by the persons authorized to do so by shareholder or director vote, or by officers acting within the authority given them by corporate law, the charter, and the by-laws. This does not pose a problem when an officer named in the resolutions is the one who executes the documents. Sometimes, however, counsel discovers that the officers who show up at the closing are not the ones named in the resolutions. When that happens, counsel must determine whether the officers attending the closing have the authority from some other source to execute the agreement or instrument on the corporation's behalf. Corporate statutes sometimes confer authority on particular officers to execute certain sorts of agreements such as contracts conveying an interest in real estate<sup>22</sup> and in recent years judge-made law has been generous about the implied powers of presidents.<sup>23</sup>

When they are faced with a resolution conferring authority only on the president and perhaps a few other top officers such as an executive vice president—as resolutions often do when they confer authority to act on a significant

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21. Opinions often confirm that the debt instrument conforms to the requirements of the indenture. One form of opinion, for example, states that "the bonds are in the form contemplated by the indenture and have been duly authorized, executed, authenticated, issued and delivered." Alternatively, opinions sometimes state that "the bonds are in due and proper form." Sometimes, authentication by the trustee is expressly assumed.

22. See, e.g., MASS. GEN. L. ch. 156B, § 115 (1984).

Any recordable instrument purporting to affect an interest in real estate, executed in the name of a corporation by the president or a vice president and the treasurer or an assistant treasurer, who may be one and the same person, shall be binding on the corporation in favor of a purchaser or other person relying in good faith on such instrument notwithstanding inconsistent provisions of the articles of organization, certificate of incorporation, charter, special act of the corporation, constitution, by-laws, resolutions or votes of the corporation.

*Id.*

23. R. CLARK, CORPORATE LAW § 3.3.1. (1986).

[T]he office of corporate secretary by itself, is not generally considered to give the holder of it authority to bind the corporation . . . . The treasurer also has no implied authority to bind the corporation in most jurisdictions . . . . Vice presidents are an even less favored lot; some cases say that they have no authority simply by the virtue of their office. As for corporate presidents, the older cases took the niggardly view that a corporate president's implied authority consisted only of the power to preside at director and shareholder meetings. But later cases, reacting to the obvious force of custom, began to recognize that corporate presidents usually should be viewed as having the powers of a general manager and, therefore, authority to bind the corporation in all ordinary business transactions.

*Id.* (citations omitted).

matter—lawyers will have difficulty concluding that an officer who is not named may properly execute the contract. Courts have been less generous in implying powers of vice presidents, treasurers, and secretaries.<sup>24</sup> In any event, the specificity of the resolutions may well reflect an intention to limit authority to the named individuals.

The lawyer's job is not necessarily completed, however, even if the "right people" appear at the closing. Authorizing resolutions typically extend authority to sign to designated officers such as "the President" rather than to named individuals.<sup>25</sup> Thus, the question arises whether the lawyer must confirm that the person signing was duly elected to and incumbent in the designated office. Lawyers, especially special counsel retained for the transaction, may rely on incumbency certificates for this purpose. Company counsel, on the other hand, sometimes prefer to supplement an incumbency certificate with their own review of the corporate records. When a corporate record check reveals that the purported officer was not duly elected, the lawyer might be able, depending on the circumstances, to give the opinion either on the theory that subsequent board actions implicitly ratified the election or on the theory that the directors intended to authorize the individual they thought held the named office to sign on behalf of the corporation regardless of defects in his election. Time permitting, however, the course most lawyers prefer is to have the directors ratify the election or adopt a new resolution extending authority to sign to named individuals. The lawyer could not give an unqualified "duly executed" opinion if the persons signing the agreement or instrument lacked actual authority to bind the company, even though the agreement or instrument might be enforced against the company under a doctrine such as apparent authority.<sup>26</sup> The opinion should not depend on what the opinion recipient knows or does not know about the authority of the person executing the agreement.

### 3. *Duly Delivered*

The "duly delivered" portion of the opinion confirms that the corporation has taken such other steps as may be required to bring the agreement or instrument into effect.<sup>27</sup> Normally, this is done by handing over a signed agreement or

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24. *Id.*

25. Resolutions typically extend authority to "the officers," to "proper officers," or to the holders of specific offices ("the President or any Vice President"). A resolution covering "the officers" generally has the disadvantage of possibly according discretionary authority to a lower-level officer such as an assistant secretary whose duties are purely ministerial. The "proper officer" formulation leaves open the question of what officers are "proper" and, thus, ought not to be used unless the answer to that question is clear because, for example, a statute identifies what officers must act. Naming specific offices in the resolution is the least ambiguous and has the advantage of limiting discretionary authority to officers expressly identified by the board.

26. For an extensive discussion of the apparent authority of corporate officers under New York law, see *General Overseas Films, Ltd. v. Robin Int'l, Inc.*, 542 F. Supp. 684, 695-96 (S.D.N.Y. 1982), *aff'd*, 718 F.2d 1085 (2d Cir. 1983) (holding that a corporate treasurer lacked apparent authority to bind the corporation to a guaranty of substantial obligations of another company).

27. U.C.C. § 1-201(14) (1978) provides that "[d]elivery, with respect to instruments, documents of title, chattel paper, or certificated securities means voluntary transfer of possession." The *California Report*, *supra* note 3, at 1036, states, "'Duly delivered' means that the company has delivered the agreement to the other party or parties to the transaction to create a binding contract."

instrument at the closing. Physical delivery of the instrument or agreement, however, is not the whole story. In a complex transaction, dozens of closing documents typically are assembled at a lengthy preclosing, and a full set of executed documents is entrusted to the parties' respective lawyers for release to their clients the following day. Even though physical delivery already has taken place at the preclosing, the lawyer cannot give the opinion until each party has authorized release of the documents.

A more difficult question arises when all the documents are located in the office of counsel for one party and the opinion must be rendered before a set of executed documents is handed over to the other party. Once both parties have instructed counsel to release the documents, lawyers are usually willing to give the "duly delivered" opinion—even though no physical transfer has occurred—on the theory that the lawyer holding the documents has become the bailee for the other party.

### B. "Legal, Valid and Binding"

Opinions on debt instruments, and many opinions on agreements, state that they are "legal, valid and binding obligations of the Company" or use similar phrases such as "valid and legally binding" or simply "valid and binding." The "legal, valid and binding" portion of the opinion means that a court would recognize the company's obligations under the agreement or instrument as lawful and would allow damages or grant some other remedy in the event of a violation.<sup>28</sup> The term "valid" appears in almost all such opinions and confirms compliance with contract law requirements for the formation of a contract. The term "binding" also appears in most opinions and confirms that the agreement or instrument imposes obligations on the company for which it could be held legally accountable. The term "legal" confirms compliance with law, and so is subsumed in the terms "valid" and "binding." Leaving that term out, therefore, makes the opinion less explicit but no easier to give.<sup>29</sup>

A preliminary and important question is whether the opinion relates to every obligation of the company contained in the agreement or instrument or only to material obligations. Some lawyers take the absolutist position that the opinion cannot be given unless every obligation of the company is legal, valid and

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28. See Case & Bernstein, *supra* note 3, at 3.

[Legal, valid and binding means] that there has been created some right, some entitlement to a recovery that will be legally recognized (e.g., a claim allowable in bankruptcy or entitled to a money judgment). It does not purport to advise the addressee of what effective remedies there are or when they may be available, once the claim is allowed or judgment is obtained. In other words, [legal, valid and binding] . . . tells the addressee that he will be entitled to legal protection for the bargain but does not purport to say whether the remedy will be award of what was actually bargained for or some other relief, judicially determined to be the legal equivalent of what was bargained for, such as new securities issued in a plan of financing.

*Id.*

For a discussion of the difference between "legal, valid and binding" and "enforceable in accordance with its term," see *infra* text accompanying notes 101-10.

29. Although some lawyers omit the term "legal" to avoid redundancy, most lawyers choose to include it for purposes of clarity and to provide those who rely on the opinion protection against a claim that they were knowingly engaged in an unlawful transaction.

binding in all respects, subject only to the equitable principles and bankruptcy qualifications. These lawyers temper their positions somewhat by giving an expansive interpretation to the equitable principles and bankruptcy qualifications. The absolutist view is intended to force lawyers to do their homework by examining each clause of the agreement or instrument with a view to identifying any possible defense or excuse the company could advance for nonperformance. Leading participants in the preparation of the New York Report—a report drafted under the auspices of three New York bar associations and perhaps the leading authority on legal opinions—are strong advocates of the absolutist view.<sup>30</sup>

The California Report—a detailed analysis of legal opinions prepared under the auspices of the Committee on Corporations of the Business Law Section of the State Bar of California—takes the opposite view, maintaining that an opinion “does not mean that all provisions of the agreement are effective” or that “every provision in the agreement . . . will be upheld by a court.”<sup>31</sup> The California Report, unfortunately, does not explain which provisions are covered and which are not. Absolutists have been heard to state that they would not accept the opinion of a California lawyer who subscribed to the position taken in the California Report.

A possible middle ground takes into account the fact that all clauses are not of equal importance and that all legal problems are not of equal significance to opinion recipients. For example, a stockholder in an acquired corporation is not likely to be concerned that a covenant in the merger agreement giving it the right to inspect books and records of the merged company is limited by Department of Defense confidentiality rules restricting access to classified engineering data. The stockholder, however, would expect to be able to rely on that covenant to obtain the financial statements he would need to confirm the adequacy of payments to him under an earnout clause.<sup>32</sup> Under the middle ground approach, the opinion would apply only to material violations of the material obligations in an agreement, with materiality being measured in each case in terms of the needs of opinion recipients at the time the opinion is rendered.

Although a test that looks to materiality has much to commend it, it affords little practical help to a lawyer preparing an opinion. In many instances the opining lawyer does not represent the opinion recipient and is in no position to assess what it might and might not regard as material. Thus, the safest course, and the one followed by many if not most lawyers, is to act as though the absolutist position were the correct one and to analyze the “legal, valid and binding” status of each clause in the agreement. Should a defect later be identified, however, the materiality test will allow the lawyer to sleep nights if he can conclude that the defect was of no great consequence to the opinion recipient.

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30. *New York Report*, *supra* note 1.

31. *California Report*, *supra* note 3, at 1038.

32. Similarly, a lender may include a provision in a loan agreement permitting acceleration if an interest payment is just a day late, even though all parties understand that a court is not likely to grant acceleration under those circumstances. See *infra* text accompanying notes 93-94.

Another preliminary point is that the opinion relates to the obligations of the company rather than those of the other party to the agreement. Assume for example, that the lawyer is asked to opine that an agreement by which a company acquires all of the assets of another corporation is a "legal, valid and binding obligation" of the acquiring company. The agreement contains a noncompetition clause prohibiting the seller from engaging in a similar business anywhere in the world for a period of twenty years, a clause counsel regards as overbroad and unenforceable. Because the clause purports to bind the seller rather than the acquiring company, it ordinarily would not prevent counsel from giving the seller an unqualified opinion about the obligations of the buyer. Counsel, however, could not give the opinion without qualification if the unenforceability of the seller's obligation would prevent enforcement of the buyer's obligations under a doctrine such as failure of consideration.

Although each of the words "legal," "valid," and "binding" may have a separate meaning, they appear together in opinions and are best analyzed as a single phrase.

1. First, the opinion confirms compliance with applicable requirements for the formation of a contract or the creation of the instrument. Thus, the opinion could not be given unless the agreement or instrument had been "duly authorized, executed and delivered" within the meaning of those phrases set forth above.<sup>33</sup> Due authorization, execution and delivery by the other party is sometimes expressly assumed in the opinion.<sup>34</sup> Opinions may state, for example:

In making our examination of documents executed by parties other than the Corporation, we have assumed that such parties had the corporate power to enter into and perform all obligations thereunder and have also assumed the due authorization by all requisite corporate action and execution and delivery of such documents and the validity and binding effect thereof.<sup>35</sup>

A leading authority takes the position that such an assumption is implicit,

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33. See *supra* text accompanying notes 5-27; see also Wolfson, *Opinions of Counsel to the Underwriters in Public Offerings of Securities*, in *OPINION LETTERS OF COUNSEL 1985*, *supra* note 3, at 79, 96 (it is "[p]robably generally agreed that . . . binding agreement must have been duly authorized, executed and delivered.")

Notes or other instruments that have not been "duly authorized," nevertheless, might be "legal, valid and binding" if they were held by a bona fide purchaser who lacked notice or knowledge of the defect. The lawyer will rarely if ever be able to give an unqualified opinion on this basis, however, because the phrase "legal, valid and binding" is almost always accompanied by "duly authorized, executed and delivered."

34. For a case holding that a stockholders' agreement did not bind one party because of the lack of authority of someone purporting to sign on behalf of another party, see *Winter v. Skoglund*, Nos. C5-86-637, C7-86-848 (S. Ct. Minn., Apr. 17, 1987).

35. *New York Report*, *supra* note 1, at 1899. Another version states:

You have not asked us to pass upon your power and authority to enter into the Agreement or to effect the transactions contemplated thereby, and for the purposes of this opinion we have assumed that you have all requisite power and authority and have taken all necessary corporate or other action to enter into the Agreement and to effect such transactions.

even if it is not expressly stated, and suggests that it not be included in the opinion.<sup>36</sup> Many firms follow this practice.<sup>37</sup>

In addition, the lawyer must assure himself that the agreement or instrument complies with any contract law requirements with respect to form. The opinion could not be given, for example, about an oral agreement for the sale of land when the statute of frauds requires that such an agreement be in writing. Similarly, the opinion could not be given about an agreement that was unenforceable because it failed to comply with the Uniform Commercial Code's requirement that contracts for the sale of securities state the quantity and price and be in writing and signed by the party against whom enforcement is sought.<sup>38</sup>

The opinion also confirms that the agreement or instrument is not so incomplete, vague, or confusingly drafted that a court would refuse to give effect to the company's obligations. Even careful businessmen and lawyers sometimes forget to cover important matters, and skilled negotiators sometimes settle on vague language, leaving some problems to be resolved if and when they arise. When contract language on important matters is "so indefinite as to make it impossible for a court to fix the legal liability of the parties" or when essential matters are omitted altogether, courts may conclude that no enforceable agreement exists.<sup>39</sup> Under those circumstances, the lawyer could not,

36. *New York Report*, *supra* note 1, at 1899 ("The Committee believes that whether or not the opinion so states, a lawyer may make assumptions along the lines indicated above and should not be held to have opined by implication that other parties to an agreement are bound. Opinions by implication should not be furnished or sought. The Committee prefers to omit assumption language such as that shown above."). The language referred to is that quoted in the text of this Article. This view is also expressed by Babb, Barnes, Gordon & Kjellenberg, *supra* note 3, at 564.

37. Wolfson, *supra* note 33, at 96 ("[the] binding effect [of the agreement] on all parties other than designated party [is] generally assumed and, commonly, [the] assumption is unstated.').

38. The Uniform Commercial Code provides that:

A contract for the sale of securities is not enforceable by way of action or defense unless:

- (a) there is some writing signed by the party against whom enforcement is sought or by his authorized agent or broker, sufficient to indicate that a contract has been made for sale of a stated quantity of described securities at a defined or stated price . . . .

U.C.C. § 8-319(a) (1978). Furthermore, a contract for sale of securities is not enforceable unless delivery has been accepted, confirmation of the transactions has been received and not objected to, or the party against whom enforcement is sought admits that a contract was made. *Id.* § 8-319(b)-(d); see *Jennison v. Jennison*, 499 A.2d 302 (Pa. Super. 1985) (refusing specific performance of a stock purchase agreement that did not specify price); *Pitts v. Halifax Country Club, Inc.*, 19 Mass. App. 525, 531-32, 476 N.E.2d 222, 227 (1985) (stating, in dictum, that an oral agreement to repurchase stock was not binding). Under the law of some states shares of the stock of closely-held corporations may not be "securities" for Article 8 purposes. See HAWKLAND, ALDERMAN & SCHNEIDER, U.C.C. SERIES § 8-101:02 (1986). Some corporate statutes impose similar requirements for stock subscription agreements. See, e.g., DEL. CODE ANN. tit. 8, § 166 (1983).

39. *Moore v. Dilworth*, 142 Tex. 538, 542-43, 179 S.W.2d 940, 942 (1944).

It is essential to the validity of a contract that it be sufficiently certain to define the nature and extent of its obligations. If an agreement is so indefinite as to make it impossible for a court to fix the legal liability of the parties thereto, it cannot constitute an enforceable contract.

*Id.*; See *Transamerica Equip. Leasing Corp. v. Union Bank*, 426 F.2d 273 (9th Cir. 1970) (holding that an oral agreement by a bank to extend a loan was unenforceable because it failed to include the

however, give the "legal, valid and binding" opinion. When the vagueness or omission is less crucial, courts often supply interpretations or construct terms based on custom, commercial practice,<sup>40</sup> prior dealings between the parties, the implications of other portions of the contract, rules of language, and principles of reason and fairness.<sup>41</sup> In contracts for the sale of goods, some supplementary terms are provided by the Uniform Commercial Code.<sup>42</sup> Normally, the lawyer can give the "legal, valid and binding" opinion even though the terms of the agreement may be supplemented by such interpretive techniques. However, if the lawyer concludes that courts will interpret the company's obligations more narrowly than the opinion recipient reasonably believes, he should as a matter of good practice disclose this point to opinion recipients.

The opinion also confirms that courts would not refuse to give effect to the agreement or instrument on the grounds that it was only preliminary in nature.<sup>43</sup> Courts may refuse, for example, to enforce the terms of a letter of

repayment schedule). *But see* *Texaco, Inc. v. Pennzoil Co.*, No. 01-86-0216—CV (Tex. Ct. App. Feb. 12, 1987).

Section 33 of the RESTATEMENT (SECOND) OF CONTRACTS provides:

(1) Even though a manifestation of intention is intended to be understood as an offer, it cannot be accepted so as to form a contract unless the terms of the contract are reasonably certain.

(2) The terms of a contract are reasonably certain if they provide a basis for determining the existence of a breach and for giving an appropriate remedy.

RESTATEMENT (SECOND) OF CONTRACTS § 33 (1979).

Courts may provide relief under doctrines such as those relating to unjust enrichment, restitution, and promissory estoppel even when they conclude that no contract has been entered into. A lawyer could not give an unqualified "legal, valid and binding" opinion about an agreement courts would refuse to enforce as a matter of contract law even if relief were available under some such doctrine.

40. *See* *Mid-Continent Telephone Corp. v. Home Telephone Co.*, 319 F. Supp. 1176, 1193 (N.D. Miss. 1970) (holding that a merger agreement was enforceable notwithstanding its failure to specify whether the transaction was to be conducted pursuant to registration with the SEC. The court relied on "a well-known custom in the area of corporate mergers . . . to issue unregistered stock . . .").

41. *See* *American Cyanamid Co. v. Elizabeth Arden Sales Corp.*, 331 F. Supp. 597, 603-04 (S.D.N.Y. 1971) (stating that a letter agreement providing for the sale of all of a corporation's assets had "the essential elements with respect to subject matter required for a contract" even though it failed to specify the closing date — "[a] reasonable time may be implied" — and omitted representations, warranties, and various other matters); E. FARNSWORTH, *CONTRACTS* § 3.29, at 205-06 (1982); RESTATEMENT (SECOND) OF CONTRACTS § 204 (1979) ("When the parties to a bargain sufficiently defined to be a contract have not agreed with respect to a term which is essential to a determination of their rights and duties, a term which is reasonable in the circumstances is supplied by the court . . ."); U.C.C. § 2-204(3) (1978) ("[e]ven though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.); *see also id.* § 2-305 (providing a similar rule for instances where the price is left undetermined).

Courts may award damages for violations of contracts even when they are so indefinite that specific performance is not available. *See infra* text accompanying notes 104-05.

42. U.C.C. § 2-305(1)(a) (1978) (providing that "[t]he parties if they so intend can conclude a contract for sale even though the price is not settled. In such a case the price is a reasonable price at the time for delivery if . . . nothing is said as to price . . ."); *id.* § 2-309 (1) (providing that the time for delivery, if not agreed upon, "shall be a reasonable time." U.C.C. § 2-308(a) provides that "[u]nless otherwise agreed . . . the place for delivery of goods is the seller's place of business or if he has none his residence."); *id.* § 2-310(a) (providing that "[u]nless otherwise agreed . . . payment is due at the time and place at which the buyer is to receive the goods . . .").

43. *See, e.g., Jennison v. Jennison*, 346 Pa. Super. 47, 499 A.2d 302 (1985) (refusing specific performance of an agreement to sell stock because the price had not been agreed upon). Vagueness,



intent on the grounds that the parties did not mean it to constitute their final understanding on the matter,<sup>44</sup> although as *Texaco, Inc. v. Pennzoil* demonstrates, courts sometimes hold parties to their handshake agreements even in billion dollar transactions.<sup>45</sup>

Special problems of incompleteness, vagueness, or lack of finality are presented by agreements such as construction contracts, distributorship and franchise

incompleteness, and ambiguity alone sometimes lead courts to conclude that the agreement is not final. *See, e.g., Sisk v. Parker*, 469 S.W.2d 727, 733 (Tex. Civ. App. 1971) (holding that an agreement to form a corporation and cause it to obtain financing and construct apartment buildings constituted "no more than an agreement to agree in the future on essential terms" in view of the fact that many "essential elements," such as the capital structure of the corporation and the amount of the loan, were left unresolved by the contract).

44. *See, e.g., Reprosystem, B.V. v. SCM Corp.* 727 F.2d 257 (2d Cir.), *cert. denied*, 469 U.S. 828 (1984) (holding that no contract was created by an "agreement in principle" or by "final drafts" of an agreement). The *Reprosystem* court described New York law as follows:

Although "[c]ontract law has progressed and evolved sounder principles since the days of ritualistic and formalistic sealed instrument requirements," there are still situations where the absence of a signed, formal agreement is fatal to an argument that a contract exists. This court [has] summarized the alternative New York rules on this subject [as] . . . .

First, if the parties intend not to be bound until they have executed a formal document embodying their agreement, they will not be bound until then; and second, the mere fact that the parties contemplate memorializing their agreement in a formal document does not prevent their informal agreement from taking effect prior to that event. \*\*\* These rules, placing the emphasis on intention rather than form, are sensible and reasonable.

. . . [We have held that] the party invoking the first rule of New York contract law described above must prove either that both parties understood they were not to be bound until the executed contract was delivered, or that the other party should have known that the disclaiming party did not intend to be bound before the contract was signed.

727 F.2d at 261 (citations omitted) (quoting *V'Soske v. Barwick*, 404 F.2d 495, 499 (2d Cir. 1968), *cert. denied*, 394 U.S. 921 (1969)). Among the facts relied on by the *Reprosystem* court for the conclusion that the drafts did not constitute a contract was the fact that:

the drafts of the . . . [agreement] provided "when executed and delivered, this . . . [agreement] will be a valid and binding agreement \* \* \* in accordance with its terms." Despite their many other differences over the proposed contracts, neither party took exception to these provisions that conditioned their binding effect on formal execution and delivery. Thus, the contract drafts, combined with the parties' other written communications, conclusively establish a mutual intent not to be bound prior to execution of the formal documents . . . .

*Id.* at 262. A subsequent, similar description of New York law on this point is contained in *Winston v. Mediafare Entertainment Corp.*, 777 F.2d 78 (2d Cir. 1985) (refusing to enforce a settlement agreement).

A special problem is presented by an agreement that is in most respects clear and final, but which contains a preliminary or incomplete understanding about particular matters. *See, e.g., Scott v. Ingle Bros. Pac., Inc.*, 489 S.W.2d 554, 557 (Tex. 1972) (holding that when an acquisition contract referred to a nonexistent employment agreement the jury should decide whether the employment arrangements were enforceable).

45. *Texaco, Inc. v. Pennzoil, Co.*, No. 01-86-0216-CV (Tex. Ct. App. Feb. 12, 1987) (holding that Pennzoil was entitled to damages from Texaco as a result of Texaco's interference with a stock acquisition agreement between Pennzoil and Getty Oil Company even though the final acquisition agreement had not been prepared or signed); *see Mid-Continent Tel. Corp. v. Home Tel. Co.*, 319 F. Supp. 1176, 1189-92 (N.D. Miss. 1970) (holding that a letter agreement to engage in a "C" reorganization constituted a binding contract under Mississippi law).

agreements, employment agreements, and joint ventures. "Relational contracts"<sup>46</sup> such as these, often express the parties' duties vaguely or leave them to be determined later based on further decisions by one or both parties.<sup>47</sup> Some courts are willing to enforce such contracts even when they are indefinite on crucial points<sup>48</sup> and impose generally worded obligations such as a duty to use "best efforts"<sup>49</sup> or to conform to a standard of "reasonableness."<sup>50</sup>

The opinion also confirms that consideration requirements have been satisfied.<sup>51</sup> Usually this is not a problem because the exchange of promises in the agreement is itself adequate consideration for both sides. Counsel must confirm that the promises are not illusory,<sup>52</sup> as might be the case when a line of credit

46. Works on relational contracts include: Goetz & Scott, *Principles of Relational Contracts*, 67 VA. L. REV. 1089 (1981); Macneil, *Contracts: Adjustment of Long-Term Economic Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 NW. U.L. REV. 854 (1978).

47. E. FARNSWORTH, *supra* note 41, § 3.28, at 198-99. Sometimes the parties leave an important term to be fixed unilaterally by one of the parties. The most common illustration occurs when the agreement gives a buyer of goods the right to make a later selection within a specified range of seller's stock according to grade, color, weight, or the like. When the party with the power to select is the plaintiff, no problem arises. But when the defendant has the power and refuses to make the selection, a question of definiteness arises. Some support can be found for each of three solutions. First, the agreement is not enforceable against that party. Second, the agreement is enforceable, and recovery is to be based on whatever selection would have minimized the damages. Third, the agreement is enforceable, and recovery is to be based on a selection made in good faith by the plaintiff.

*Id.* (citations omitted). For a discussion of the "agreement to agree" that leaves unsettled matters to be decided by both parties, see *id.* § 3.29.

48. See, e.g., *Mantell v. Int'l Plastic Harmonica Corp.*, 141 N.J. Eq. 379, 389, 55 A.2d 250, 256 (1947) (holding a distributorship agreement enforceable even though no price was set. The court stated, "[i]n the very nature of the exclusive sales and distribution contract, it is not usually practicable to fix prices and the quantum of goods sold; and the rules of certainty and definiteness which govern the ordinary contract of sale have no application."). Cf. *Mid-Continent Tel. Corp. v. Home Tel. Co.*, 319 F. Supp. 1176, 1192 (N.D. Miss. 1970) (holding that a letter agreement to engage in a "C" reorganization was binding and stating that "Mississippi has recognized that where the nature of the situation prevents precise advance designation of details, somewhat less precision is required . . .").

49. See, e.g., *Bloor v. Falstaff Brewing Corp.*, 601 F.2d 609 (2d Cir. 1979). *But see Kraftco Corp. v. Kolbus*, 1 Ill. App. 3d 635, 274 N.E.2d 153 (1971).

50. See, e.g., *Corthell v. Summit Thread Co.*, 132 Me. 94, 167 A. 79 (1933) (holding an employer bound by a contract that required him to provide "reasonable recognition" to an employee in return for the employee's promise to turn over rights to his future inventions). *But see Varney v. Ditmars*, 217 N.Y. 223, 111 N.E. 822 (1916) (refusing to allow recovery under a promise by an employer to pay an employee "a fair share of my profits").

51. Sometimes the presence of a seal satisfies consideration requirements. S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 109 (3d ed. 1961 & Supp. 1979).

52. See *Blish v. Thompson Automatic Arms Corp.*, 30 Del. Ch. 538, 569, 64 A.2d 581, 597 (1948).

. . . [T]he [underwriting] agreement provides for cancellation by [the underwriters] "if prior to the closing date, in your absolute judgment, political, economic or market conditions are such as to render the contemplated public offering of the common stock or consumation of the sale of the common stock to the public, or both, impractical or inadvisable." It is from this language that the appellant asserts her claim of lack of mutuality . . . . This contention cannot be sustained. The question involved is one of good faith, proper motive and fair dealing, which by express terms or by implication is written into every contract. The term "absolute judgment," as indicated, means a judgment based upon sincerity, honesty, fair dealing and good faith . . . .

can be revoked at any time at the lender's discretion<sup>53</sup> or when an executory distributorship agreement is terminable at will by either party.<sup>54</sup> Some older cases hold that requirements contracts are illusory,<sup>55</sup> but courts often avoid this conclusion by interpreting the contract to require the purchaser to act in good faith.<sup>56</sup> When there is no exchange of promises, counsel must confirm receipt of consideration in some other form. Counsel could not, for example, give the "legal, valid and binding" opinion about options to purchase stock unless consideration had been given for the options,<sup>57</sup> or about a note under a revolving credit agreement until funds had been taken down. By way of contrast, counsel could give an opinion about the revolving credit agreement itself if the prospective borrower has paid standby or other fees to the lender.

2. Second, the opinion confirms that as of its date the obligations of the company remain in effect. The lawyer could not give the "legal, valid and

53. A similar problem might be presented by loan agreements that permit the lender to accelerate the obligation at will. But U.C.C. § 1-208 (1978), provides that:

A term providing that one party . . . may accelerate payment or performance . . . "at will" or "when he deems himself insecure" or in words of similar import shall be construed to mean that he shall have power to do so only if he in good faith believes that the prospect of payment or performance is impaired.

The Official Comment to § 1-208 states:

The increased use of acceleration clauses either in the case of sales on credit or in time paper or in security transactions has led to some confusion in the cases as to the effect to be given to a clause which seemingly grants the power of an acceleration at the whim and caprice of one party. This Section is intended to make clear that despite language which can be so construed and which further might be held to make the agreement void as against public policy or to make the contract illusory or too indefinite for enforcement, the clause means that the option is to be exercised only in the good faith belief that the prospect of payment or enforcement is impaired.

This approach was extended in *K.M.C. Co. v. Irving Trust Co.*, 757 F.2d 752 (6th Cir. 1985), where the court held that a lender could not refuse without notice to extend funds under a line of credit agreement unless it did so in good faith. *K.M.C.*, however, involved a line of credit that largely had been taken down.

54. See, e.g., *Kraftco Corp. v. Kolbus*, 1 Ill. App. 3d 635, 274 N.E.2d 153 (1971).

55. See, e.g., *Crane v. C. Crane & Co.*, 105 F. 869, 871-72 (7th Cir. 1901); *Cohen v. Clayton Coal Co.*, 86 Colo. 270, 281 P. 111 (1929). A similar problem is presented by supply contracts under which the buyer promises to acquire all of a company's output.

A Delaware decision suggests that a "white knight's" promise to merge with a target company constituted illusory consideration when the agreement was intended to defeat a hostile takeover bid and was contingent on that bid's not being successful. *DMG, Inc. v. Aegis Corp.* No. 7619 (Del. Ch., June 29, 1984), *reprinted in* 9 DEL. J. CORP. L. 437, 442 (1984).

56. E. FARNSWORTH, *supra* note 41, § 7.17, at 527-28. See U.C.C. 2-306(1) (1978):

A term which measures the quantity by the output of the seller or the requirements of the buyer means such actual output or requirements as may occur in good faith, except that no quantity unreasonably disproportionate to any stated estimate or in the absence of a stated estimate to any normal or otherwise comparable prior output or requirements may be tendered or demanded.

*Id.*

57. Questions about the consideration given for options granted under employee stock option plans usually are resolved by making the options exercisable only after a specified period of employment. See *Kerbs v. California Eastern Airways*, 90 A.2d 652 (Del. 1962); *Gottlieb v. Heyden Chemical Corp.*, 90 A.2d 660 (Del. 1952); *cf.* E. FARNSWORTH, *supra* note 41, § 3.23, at 172 (Offers may be made irrevocable if supported by consideration. "[W]hatever hostility may have been shown to the device of nominal consideration in general, courts have tolerated that device as a means of making an offer irrevocable and upheld options for which the peppercorn is as little as a dollar.").

binding” opinion if obligations of the company had been altered by express or implied amendment or by waiver. This presents few difficulties when, as is often the case, the opinion is given at the time the agreement is entered into and the agreement contains a clause stating that it constitutes the entire understanding between the parties.<sup>58</sup>

The opinion raises more difficult questions when it is given some time after the agreement was executed. For example, at the time of the second takedown under a revolving credit agreement. Under those circumstances, the lawyer must take care to identify any amendments and waivers<sup>59</sup> and to specify in the opinion precisely which documents are covered. The lawyer also must confirm that the obligations of the company set forth in the agreement or instrument have not been extinguished by performance<sup>60</sup> or by the statute of limitations. Lawyers often obtain officers’ certificates attesting to the current status of such an agreement or instrument.

Estoppel presents a harder case. A party to an agreement may, through its conduct, forfeit the right to enforce the other party’s obligations. By regularly accepting late interest payments without objection, for example, a lender might become estopped to accelerate the loan for late payments in the future.<sup>61</sup> Because of the difficulty of ascertaining whether such conduct has occurred, counsel ought to be able to give an unqualified “legal, valid and binding” opinion unless he knows of facts that would clearly excuse the company from performing its obligations.

3. Third, the opinion confirms that a court would give effect to the obligations of the company set forth in the agreement or instrument.<sup>62</sup>

a. Illegality and contravention of public policy.—The “legal, valid and binding” opinion confirms that courts would not refuse to recognize the existence of the agreement or instrument or to hold the company to account on the grounds that its provisions, whether substantive, procedural, or remedial, were illegal or contrary to public policy.<sup>63</sup>

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58. *But see* K.M.C., Inc. v. Irving Trust Co., 757 F.2d 752 (6th Cir. 1985) (holding that a borrower’s contractual waiver of the right to a jury trial was unenforceable because the lender gave oral assurances that the waiver provision would not be enforced). The decision was based on the constitutional protection of the right to a jury trial. *Id.* at 755-58. Counsel is entitled to rely on the representation of the parties that the written agreement constitutes their entire understanding unless he is aware of an agreement—written or oral—to the contrary.

59. Loan agreements often provide that no implied waiver shall be given effect.

60. The lawyer can give an unqualified “legal, valid and binding” opinion when the company has performed only obligations that by the terms of the agreement or instrument fell due prior to the date of the opinion, such as interest under a note.

61. *Skendzel v. Marshall*, 261 Ind. 226, 301 N.E.2d 641, *cert. denied*, 415 U.S. 921 (1973).

62. For a discussion about which obligations are covered, see *supra* text accompanying notes 28-32.

63. When evaluating questions of legality and contravention of public policy, the lawyer should consider which law governs—for example the law of the place of performance, the law selected in the contract, the law of the place where the contract was executed or the law of the state or states where the parties reside.

According to one leading authority, a lawyer could give the opinion unless the violation of law would make the obligation of the company void or voidable. See *New York Report, supra* note 1, at 1916. A similar approach is taken in *Babb, Barnes, Gordon & Kjellenberg, supra* note 3, at 564:

[E]ven though the expressions ‘valid’, ‘enforceable’ and ‘binding’ are not generally construed to negative all defenses to a contract action, this opinion does cover the

i. Substantive Terms.—The lawyer could not give the “legal, valid and binding” opinion about an agreement or instrument containing substantive terms that courts would refuse to enforce on the grounds that they violated the law or public policy:<sup>64</sup> For example a gambling contract, a contract under which the company agreed to bribe government officials, a note carrying a usurious rate of interest,<sup>65</sup> a voting trust that violated the requirements of a corporate

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non-availability of certain defenses of the Company to an action on the Agreement, e.g. . . . non-contravention of a statute or common law rule declaring an essential term in the Agreement void on its face.

This approach fails to give due weight to concerns of an opinion recipient about penalties other than voidness or voidability—for example, fines and injunctions.

64. Many jurisdictions look to the facts and circumstances of each case to decide whether to enforce a contract that is illegal or contrary to public policy. Under this approach, courts consider factors such as the sophistication of the parties and their knowledge of the illegality, and whether the plaintiff or the defendant is the party sought to be protected by the law or public policy in question. See, e.g., *Lewis & Queen v. N.M. Ball Sons*, 48 Cal. 2d 141, 150-53, 308 P.2d 713, 719-20 (1957) (Traynor, J.):

[C]ourts generally will not enforce an illegal bargain or lend their assistance to a party who seeks compensation for an illegal act. The reason for this refusal is not that the courts are unaware of possible injustice between the parties, and that the defendant may be left in possession of some benefit he should in good conscience turn over to the plaintiff, but that this consideration is outweighed by the importance of deterring illegal conduct . . . .

In some cases, on the other hand, the statute making the conduct illegal, in providing for a fine or administrative discipline excludes by implication the additional penalty involved in holding the illegal contract unenforceable; or effective deference is best realized by enforcing the plaintiff's claim rather than leaving the defendant in possession of the benefit; or the forfeiture resulting from unenforceability is disproportionately harsh considering the nature of the illegality. In each such case, how the aims of policy can best be achieved depends on the kind of illegality and the particular facts involved.

. . . [W]hen the Legislature enacts a statute forbidding certain conduct for the purpose of protecting one class of persons from the activities of another, a member of the protected class may maintain an action notwithstanding the fact that he has shared in the illegal transaction. The protective purpose of the legislation is realized by allowing the plaintiff to maintain his action against a defendant within the class primarily to be deterred. In this situation it is said that the plaintiff is not *in pari delicto*.

*Id.*

*Lewis v. Queen* was quoted with approval in *Bodily v. Parkmont Village Green Home Owners Assoc., Inc.*, 104 Cal. App. 3d 348, 357, 163 Cal. Rptr. 658, 663 (1980). See also *California Pac. Bank v. Small Bus. Admin.*, 557 F.2d 218 (9th Cir. 1977) (containing an interesting discussion of the extent to which a regulatory agency that condones an illegal contract is estopped to use the defense of illegality); *Lowenschuss v. Kane*, 520 F.2d 255, 264-67 (2d Cir. 1975) (holding that when a tender offer was enjoined because of defects in the disclosure documents, the offeror might nevertheless be liable in contract to tendering shareholders if the facts making the offer illegal were known to the offeror but not “reasonably expected to be known” to plaintiff); RESTATEMENT (SECOND) OF CONTRACTS §§ 178-185 (1979).

This raises the question whether under “facts and circumstances” favorable to enforcement the lawyer could give an unqualified “legal, valid and binding” opinion even when a material obligation of the company was contrary to law or public policy. Some lawyers might be tempted to give the opinion (perhaps without the word “legal”) on the grounds that enforceability is the only issue that really matters. In most situations, however, a qualification pointing out the problem and the uncertainty inherent in a test based on a judge's assessment of the facts or circumstances would appear to be preferable.

65. Statutes that prohibit usury often put a ceiling on the lender's charges generally. See

statute,<sup>66</sup> or a stock transfer restriction agreement that was "unreasonable" and, therefore, would not be enforced under judge-made corporate law.<sup>67</sup> The lawyer could not give the "legal, valid and binding" opinion about an agreement or instrument that imposed obligations on the company that could be legally performed under some circumstances but not under others, such as a variable-rate note that would be usurious at some interest rates.<sup>68</sup>

A special case is presented by an agreement or instrument that is legal on its face but that plays a part in an illegal scheme, such as a loan agreement the borrower plans to use to finance illegal activities, a merger agreement that forms part of a scheme to create a monopoly, a tax shelter limited partnership entered into with the intent to assist in violations of the Internal Revenue Code, or an agreement among some stockholders that is intended to assist in defrauding the other stockholders. Of course, if the lawyer knows that his opinion will be used to further the illegal purpose, he cannot render the opinion.<sup>69</sup> Typically, however, the lawyer does not know of the unlawful aspects of the transaction. In such cases a distinction must be drawn between agreements and instruments that can be performed legally but may form a part of an illegal scheme and those that *require* the performance of an illegal act, such as a usurious loan agreement or a price-fixing contract. The lawyer can give an unqualified "legal, valid and binding" opinion about agreements or instruments that *can* be performed legally and consistently with public policy so long as the lawyer has no reason to know of their illegal purpose.

Another special case is presented by agreements and instruments that can be legally performed only if a license or other regulatory approval is obtained, such as a contract under which a utility agrees to engage in a stock offering that requires approval by the Department of Public Utilities. If the agreement states that the company's obligations are contingent on such approval, the lawyer can give an unqualified opinion. If it does not, the opinion should be qualified to reflect that requirement.<sup>70</sup>

A hard question is whether an opinion that an agreement to sell securities

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*e.g.*, MASS. GEN. L. ch. 271, § 49 (1984). Therefore, the lawyer may have to worry not only about interest but also about fees and expenses.

66. *E.g.* DEL. CODE ANN. tit. 8, § 218 (1986).

67. See R. CLARK, *supra* note 23, § 18.2.4.

68. When the opinion relates to securities carrying a floating rate of interest, it often contains the following qualification: "We express no opinion with respect to the validity or enforcement of the securities in the event the rate of interest provided for thereon exceeds the maximum rate from time to time permissible under applicable state and federal usury laws." Wolfson, *supra* note 33, at 101-02.

69. See Fuld II, *supra* note 3, at 1312:

An opinion that "an agreement is legally binding" probably indicates a judgment that the entire agreement is lawful. But suppose the lawyer believes that an acquisition agreement may violate the antitrust laws? Or that part of the proceeds of a loan agreement may be used for an improper purpose—(should the lawyer investigate the intended use)? Or an agreement for the sale of stock may not satisfy Rule 10b-5 or otherwise comply with the Securities Act of 1933, and the agreement may therefore be rescindable? It could be argued that none of these agreements is "legally binding."

70. It is "[p]robably generally agreed that [the opinion means that] there have been received all governmental approvals, licenses or permits without which obligations of [the] designated party would be void as a matter of law." Wolfson, *supra* note 33, at 96-97.

is "legal, valid and binding" covers compliance with state and federal securities laws.<sup>71</sup> Theoretically, it is hard to distinguish that body of law from any other, but in practice the matter is covered, if at all, in other sections of the standard opinion.<sup>72</sup> Thus, most lawyers believe that the "legal, valid and binding" opinion does not cover compliance with securities laws. Lawyers sometimes explicitly exclude securities law matters, or at least state securities law matters, from the "legal, valid and binding" opinion, especially when the opinion does not contain an express clause on securities law compliance. Whether or not an express disclaimer is included, however, counsel should not give an unqualified "legal, valid and binding" opinion if he knows that performance of the agreement would violate the securities laws.<sup>73</sup>

ii. Procedural and Remedial Terms.—The lawyer could not give an unqualified "legal, valid and binding" opinion about an agreement or instrument containing procedural or remedial terms that courts would refuse to enforce. Thus, the opinion could not be given about an agreement that contained an unenforceable liquidated damages provision<sup>74</sup> or an unenforceable provision waiving compliance with the Securities Act of 1933,<sup>75</sup> releasing a party prospectively from liability for its own wrongs,<sup>76</sup> requiring arbitra-

71. For a case in which a court refused to enforce the underwriter's obligations set forth in its agreement with the issuer because of defects in the registration statement, see *Kaiser-Frazer Corp. v. Otis & Co.*, 195 F.2d 838, 843-44 (2d Cir.), *cert. denied*, 344 U.S. 856 (1952).

72. For example, an opinion relating to a private placement often states that the offer and sale of the securities is "exempt from the registration requirements of the Securities Act of 1933."

73. See *infra* text accompanying note 134.

74. CAL. CIV. CODE § 1671 (West 1982) provides as follows:

(b) Except as provided in subdivision (c), a provision in a contract liquidating the damages for the breach of the contract is valid unless the party seeking to invalidate the provision establishes that the provision was unreasonable under the circumstances existing at the time the contract was made.

(c) The validity of a liquidated damages provision shall be determined under subdivision (d) and not under subdivision (b) where the liquidated damages are sought to be recovered from either:

- (1) A party to a contract for the retail purchase, or rental, by such party of personal property or services, primarily for the party's personal, family, or household purposes; or
- (2) A party to a lease of real property for use as a dwelling by the party or those dependent upon the party for support.

(d) In the cases described in subdivision (c), a provision in a contract liquidating damages for the breach of the contract is void except that the parties to such a contract may agree therein upon an amount which shall be presumed to be the amount of damage sustained by a breach thereof, when, from the nature of the case, it would be impracticable or extremely difficult to fix the actual damage.

A case discussing the California authorities is *Sacramento Sav. & Loan Ass'n. v. Superior Court*, 137 Cal. App. 3d 142, 186 Cal. Rptr. 823 (1982) (upholding a prepayment penalty).

75. Section 14 of the Securities Act of 1933, 15 U.S.C. § 77n (1982) provides that "[a]ny condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void."

76. One commentary sets forth express exclusions from the opinion relating to "the unenforceability under certain circumstances of provisions to the effect that failure to exercise or delay in exercising rights or remedies will not operate as a waiver of the right or remedy" and "the unenforceability under certain circumstances, under California or federal statutes, or court decisions,

tion,<sup>77</sup> or waiving the right to a jury trial.<sup>78</sup> Similarly, under many corporation statutes the opinion could not be given about a provision requiring a corporation to indemnify a director or officer for actions not taken in good faith and in a manner he reasonably believed to be in the best interests of the corporation.<sup>79</sup> Opinions often expressly exclude troublesome procedural or remedial provisions.

Some remedial provisions are enforceable only if they are drafted to comply with special requirements with respect to form. Indemnification provisions in boilerplate contracts, for example, will not be enforced by California courts unless they are sufficiently "clear and express."<sup>80</sup> Similarly, under the Uniform Commercial Code a disclaimer of the implied warranty of merchantability must "mention merchantability and in case of a writing must be conspicuous."<sup>81</sup>

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of provisions indemnifying, or prospectively releasing, a party against liability for its own wrongful or negligent acts or where the release or indemnification is contrary to public policy." *Weise & Duncan, Loan Transactions*, in *OPINION LETTERS OF COUNSEL 1985*, *supra* note 3, at 367, 422-23.

Provisions exonerating a party from liability for its own deliberate or willful wrong are unenforceable in some states. *See, e.g.*, CAL. CIV. CODE § 1668 (West 1982) ("All contracts which have for their object, directly or indirectly, to exempt any one from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law."). Some California decisions go even further and refuse to enforce provisions exonerating parties for simple negligence. *See, e.g.*, *Tunkl v. Regents of Univ. of Cal.*, 60 Cal. 2d 92, 98-101, 383 P.2d 441, 445-46, 32 Cal. Rptr. 33, 37-38 (1963) (adopting a multi-factor test under which a court is to consider whether the clause "concerns a business of a type generally thought suitable for public regulation;" whether "the party invoking exculpation possesses a decisive advantage of bargaining strength;" whether "[i]n exercising a superior bargaining power the party confronts the public with a standardized adhesion contract of exculpation, and makes no provision whereby a purchaser may pay additional reasonable fees and obtain protection against negligence," and if "as a result of the transaction, the person or property of the purchaser is placed under the control of the seller, subject to the risk of carelessness by the seller or his agents.") (footnotes omitted). A recent case applying the *Tunkl* factors but enforcing the exonerating provision is *Hulsev v. Elsinore Parachute Center*, 168 Cal. App. 3d 333, 214 Cal. Rptr. 194 (1985).

77. *See Wilko v. Swan*, 346 U.S. 427, 438 (1953) (holding that an agreement to arbitrate disputes under the Securities Act of 1933 was void). *But see Shearson/American Express v. McMahon*, 107 S. Ct. 2332 (1987); *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 218-19 (1985) (holding that an agreement to arbitrate claims under a customer's agreement with a broker-dealer was enforceable as to state law claims). Other arbitration clauses are sometimes unenforceable as well. *See, e.g.*, *Harris v. Iannaccone*, 193 N.Y.L.J., Apr. 17, 1985, at 1, col. 6, 2, col. 5 & 6 (N.Y. App. Div., Apr. 4, 1985) ("[A]rbitration agreements are unenforceable where substantive rights, embodied by statute, express a strong public policy which must be judicially enforced . . . . Certain areas of the law have been found to be nonarbitrable; *e.g.* federal securities laws, . . . antitrust laws, . . . child custody, . . . and distribution of an estate . . . . Discrimination is also one of these areas.") (quoting *In re Wertheim & Co. v. Halpert*, 48 N.Y.2d 681, 397 N.E.2d 386 (1979)).

78. *See National Equip. Rental, Ltd. v. Hendrix*, 565 F.2d 255 (2d Cir. 1977) (refusing to enforce the jury-waiver clause in an equipment lease agreement on the grounds that it was "set deeply and inconspicuously in the contract" and because of the inequality of bargaining power between the parties). The court stated that "the Seventh Amendment right to a jury is fundamental and . . . its protection can only be relinquished knowingly and intentionally . . . . Indeed, a presumption exists against its waiver." *Id.* at 258.

79. *See, e.g.*, DEL. CODE ANN. tit. 8, § 145 (1983 & Supp. 1986).

80. *See Ralph M. Parsons Co. v. Combustion Equip. Assoc., Inc.*, 172 Cal. App. 3d 211, 228, 218 Cal. Rptr. 170, 181 (1985) ("When the obligation for indemnity for acts other than the indemnitor's are found in a printed form contract prepared or supplied by the indemnitee, the language imposing the obligation must be clear and express.").

81. U.C.C. § 2-316(2) (1986). Section 2-316(2) provides that "to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in the case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the exclusion must be by a writing and conspicuous." *Id.*



One of the most troublesome remedial provisions is the indemnification clause in underwriting agreements in securities transactions. In these agreements, the issuer normally promises to sell—and the underwriters to buy—a specified quantity of securities. The issuer also agrees to cause a registration statement under the Securities Act of 1933 to become effective, to furnish copies of the registration statement and prospectus to the underwriters, to amend or supplement the registration statement or prospectus as required, to register the offering under state securities laws, to furnish the underwriters financial information and disclosure documents, and to pay specified costs and expenses incident to the public offering. The issuer also makes representations concerning its corporate status, business, and securities, and the information contained in the registration statement. Last, the issuer agrees to indemnify or make contribution to the underwriters in the event that such information is wrong, misleading, or incomplete in any material respect.

The enforceability of such indemnification provisions was placed in serious doubt by the 1969 decision of the United States Court of Appeals for the Second Circuit in *Globus v. Law Research Service*.<sup>82</sup> In *Globus*, the court refused to permit an underwriter to enforce its contractual right to indemnification from the issuer for liabilities arising from misstatements in an offering circular. The court noted that the underwriter had actual knowledge of the misstatements and had, therefore, “committed a sin graver than ordinary negligence.”<sup>83</sup> The court concluded that “to tolerate indemnity under these circumstances would encourage flouting the policy of the common law and the Securities Act.”<sup>84</sup>

After *Globus*, securities lawyers developed exceptions to their opinions to reflect doubts about the enforceability of indemnification provisions. Some lawyers included limiting language that referred only to federal securities law restrictions. Other lawyers included broader provisions that also referred to state securities laws and public policy concerns.<sup>85</sup> Some opinions flatly excluded the

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82. 418 F.2d 1276 (2d. Cir. 1969), *cert. denied*, 397 U.S. 913 (1970). Subsequent authorities include *Seiler v. E.F. Hutton & Co.*, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 91,632, at 99,203 (D.N.J., Aug. 15, 1984) (“The law is settled that no right to indemnity exists under the securities laws”). Item 510 of Regulation S-K requires that a Securities Act registration statement contain a statement in substantially the following terms:

Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers or persons controlling the registrant pursuant to the foregoing provisions, the registrant has been informed that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is therefore unenforceable.

17 C.F.R. § 229.510 (1986); *see also* Item 702 of Regulation S-K, 17 C.F.R. § 229.702 (1986). State securities laws also sometimes impose limitations on indemnification for securities law violations. *See Kennedy v. Josephthal & Co.*, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,204 (D. Mass., May 9, 1983); 950 Code Mass. Reg. 13.305(a)(2)(E)(iv)(a) (1986).

83. 418 F.2d at 1288.

84. *Id.*

85. One form states:

We are of the opinion that the provisions of the underwriting agreement pertaining to indemnification by the issuer of certain persons are valid and binding agreements of the issuer enforceable against it in accordance with their terms.

With respect to the enforceability of the provisions of the underwriting agreement referred to above, we express no opinion as to (i) the effect of any provision of the Securities Act of 1933, the Securities Exchange Act of 1934, as amended, any other

indemnification clause from the coverage of the "enforceable in accordance with its terms" language or dropped altogether the "legal, valid and binding and enforceable in accordance with its terms" portion of the opinion. Although the practice still varies, the trend is towards deleting the opinion that the agreement is "legal, valid and binding" and opining only that it is "duly authorized, executed and delivered."<sup>86</sup> Lawyers who follow this practice argue that the policy concerns that render indemnification provisions suspect apply equally to the representations and warranties to the extent that they shift to the issuer liabilities for defective disclosure. Such lawyers further note that the indemnification provision and the representations and warranties are the only important parts of the agreement that survive the closing at which the opinion is rendered. They, therefore, conclude that an opinion that is almost entirely vitiated by its exception is misleading and best omitted completely.<sup>87</sup>

Indemnification provisions also are frequently included in agreements to sell stock in private placements where placement agents are involved. Many lawyers think the same doubts about enforceability exist in the private placement context and modify their opinions accordingly.

The opinion also means that a court would give effect to any choice-of-law provision included in the agreement.<sup>88</sup> A hard question may arise when the

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federal securities law or state securities or blue-sky law (Acts), (ii) the effect of any rules or regulations promulgated by any state or federal regulatory authority under the Acts (Rules), (iii) the effect of any public policy as expressed in judicial decisions or pronouncements of state or federal regulatory authority under or interpreting the Acts or Rules, (iv) the availability of specific performance or any other equitable remedy (regardless of whether such question is considered in a proceeding in equity or at law), or (v) the effect of applicable bankruptcy, insolvency, moratorium and other similar laws affecting generally the enforcement of creditors' rights.

Wolfson, *supra* note 33, at 106-07. Another approach is to use the phrase "subject to limitations attributable to the federal securities laws or to public policy principles." Alexander, *Legal Opinions by Issuer's Counsel in Underwritten Public Offerings*, in *OPINION LETTERS AND RECENT DEVELOPMENTS*, *supra* note 3, at 271, 290.

86. Underwriters usually attempt to protect themselves from the risk that indemnification may not be permitted by adding to the underwriting agreement a provision requiring contribution. One court has enforced contribution rights among "equally culpable" defendants. See *Globus, Inc. v. Law Res. Serv., Inc.*, 318 F. Supp. 955, 957-58 (S.D.N.Y. 1970), *aff'd*, 442 F.2d 1346 (2d Cir.), *cert. denied*, 404 U.S. 941 (1971). Contribution provisions typically are drafted in a way that shifts almost all the liability to the issuer and thus present the same opinion difficulties. For a discussion of the distinction between indemnification and contribution, see Scott, *Resurrecting Indemnification: Contribution Clauses in Underwriting Agreements*, 61 N.Y.U. L. REV. 223 (1986).

87. Another concern is that fraudulent statements or omissions in the registration statement might render the underwriting agreement as a whole unenforceable. See Wolfson, *supra* note 33, at 106 ("If public policy, as expressed in [the] Federal Securities laws . . . limits [the] enforceability of contracts for the sale of securities on the basis of [a] materially inaccurate or incomplete registration statement, then [the] binding effect or enforceability of all provisions (not merely indemnification and/or contribution) may be questionable."); *cf.* *Kaiser-Frazier Corp. v. Otis & Co.*, 195 F.2d 838, 843-44 (2d Cir. 1952), *cert. denied*, 344 U.S. 856 (1952) (refusing to enforce the underwriter's obligations because of defects in the registration statement).

88. A case holding a choice-of-forum clause valid in a securities law matter is *Adelson v. World Transp. Inc.*, 631 F. Supp. 504 (S.D. Fla. 1986).

Choice-of-law provisions often are drafted to select the substantive law of a specified state by excluding application of that state's choice-of-law doctrines. When this is not done, before giving an unqualified opinion, counsel must determine whether the selected jurisdiction would "accept the reference" or would, under its own choice-of-law doctrines, apply the law of still another state.

opinion is limited to the law of the lawyer's own state and the contract selects the law of another jurisdiction. In that case, the lawyer at the very least is saying that in a lawsuit in the courts of his own state the choice-of-law provision would be given effect.

Because opinion recipients expect to receive assurances about more than the choice-of-law provision in an agreement or instrument, counsel whose opinion is limited to the law of his own state often obtains an additional opinion covering the law of the selected jurisdiction. Absent such an additional opinion or an express statement that only the choice-of-law provision is covered, counsel runs the risk that his "legal, valid and binding" opinion will be misunderstood to pass upon the "legal, valid and binding" status of all the provisions in the agreement or instrument under the law of the state selected.

Loan agreements and indentures often contain "acceleration provisions" which provide that the loan will fall due immediately upon the occurrence of an "event of default." Events of default may include minor violations of borrowing restrictions, temporary changes in the finances of the company that cause it to fail financial tests, and defaults under other contracts ("cross defaults"). Some agreements provide for acceleration if the lender "deems itself insecure." Section 1-208 of the Uniform Commercial Code provides:

A term providing that one party or his successor in interest may accelerate payment or performance or require collateral or additional collateral "at will" or "when he deems himself insecure" or in words of similar import shall be construed to mean that he shall have power to do so only if he in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against whom the power has been exercised.<sup>89</sup>

Similarly, some courts have imposed limitations of reasonableness and fairness on the enforceability of acceleration clauses<sup>90</sup> or refused to permit acceleration when no material impairment of the lender's security has occurred.<sup>91</sup> Some commentators have indicated that the lawyer should qualify his opinion if under applicable law courts would refuse to accelerate payment of a loan when the default was immaterial.<sup>92</sup> Consistent with this approach, California counsel regularly include the following qualification:

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89. U.C.C. § 1-208 (1978).

90. *See, e.g.*, *Brown v. Avemco Inv. Corp.* 603 F.2d 1367, 1375-80 (9th Cir. 1979).

91. *See, e.g.*, *Sahadi v. Continental Ill. Nat'l Bank & Trust Co.*, 706 F.2d 193, 196-97 (7th Cir. 1983) (holding that an immaterial delay in payment of interest would not permit lender to call the loan); *Wellenkamp v. Bank of Am.*, 148 Cal. Rptr. 379, 385-86, 582 P.2d 970, 973-76 (1978) (refusing to enforce a "due on sale" clause in a loan secured by real estate on the grounds that it constituted a restraint on alienation and, therefore, should not be enforced unless the lender showed that "enforcement is reasonably necessary to protect against impairment to its security or the risk of default").

92. *Weise and Duncan* suggest an express exclusion from the opinion for:

limitations on the right of a lender to exercise rights and remedies under the Loan Documents or impose penalties for late payments or other defaults by the borrower if it is determined that (i) the defaults are not material, the penalties bear no reasonable relation to the damage suffered by the lender as a result of the delinquencies or defaults, or it cannot be demonstrated that the enforcement of the restrictions or

A court might not enforce payment of [the obligation] upon the accelerated maturity thereof if such accelerated maturity were delivered as a consequence of the failure of the Company to perform or observe any provision of the Credit Agreement which the court determined not to be material.

Whether this qualification, in fact, is needed turns in large part on counsel's view of the breadth of the opinion. If the opinion only applies to material violations of material obligations,<sup>93</sup> this qualification is, at best, surplusage and, if anything, creates a negative implication that, except when qualified, the opinion passes upon immaterial defaults. Some qualification may be in order, however, in states where courts will not grant acceleration automatically even for a material default. Similarly, a qualification may be required when courts will give no effect, except perhaps in extreme circumstances, to a provision in the agreement permitting the lender to accelerate when it deems itself insecure.

Lawyers sometimes include in the opinion a broad exception along the following lines:

Certain of the provisions of, and some of the remedies provided for in, the [agreement] may be affected by, or may be unenforceable in whole or in part by reason of, certain laws and judicial decisions, but the application of such laws and decisions would not materially interfere with the remedy of foreclosure for money defaults or the practical realization of the benefits of the security intended to be provided by the [agreement].

Lenders often will find this exception too broad and insist that the opinion identify those provisions whose enforceability is in doubt. Liens, pledges, mortgages, and other security interests present special questions and are not discussed in this Article.

b. Inapposite terms.—Form agreements often contain terms having no relevance to the transaction. An institutional lender may insist, for example, on using its printed form of secured loan agreement in an unsecured borrowing despite the presence of inapplicable covenants requiring that the collateral be kept insured and in good condition. Normally the lawyer could not give the “legal, valid and binding” opinion under these circumstances because courts would refuse to give effect to the inapplicable terms. Sometimes the inapposite

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burdens is reasonably necessary for the protection of the creditor, or (ii) the creditor's enforcement of the covenants or provisions under the circumstances would violate the creditor's implied covenant of good faith and fair dealing.

Weise & Duncan, *supra* note 76, at 419-20 (citations omitted). Weise and Duncan suggest a “lender preferred alternative” to the above paragraph that refers to “limitations on the right of a lender under certain circumstances to impose penalties, forfeitures, late payment charges or an increase in interest rate upon delinquency in payment or the occurrence of a default . . . .” *Id.* at 421. Another authority, however, indicates that the “equitable principles” qualification may exclude certain limitations on the enforceability of acceleration clauses from the coverage of the opinion but that it does not address the question whether acceleration of indebtedness is a matter of law rather than equity. Komaroff, *supra* note 3, at 511.

93. See *supra* text accompanying note 32.

terms are so far off the mark that the company could not violate them in any way material to the other party to the agreement. Under these circumstances an unqualified opinion could be given. Usually, however, before giving the opinion lawyers insist that any inapposite terms be corrected, for example by an addendum.

c. Interested transaction.—Under some state statutes, such as section 144 of the Delaware Corporation Law, contracts with interested parties are invalid unless they are fair.<sup>94</sup> Lawyers typically do not include an express assumption about fairness in their opinions when passing on interested transactions governed by such statutes even though fairness is an element of validity. The explanation is not that an opinion on an interested transaction is intended to pass upon fairness—a factual and business matter which lawyers are ill-equipped to address—but rather that the opinion is grounded on an unstated assumption that the transaction is fair.<sup>95</sup>

When lawyers have serious doubts about fairness, they may choose to spell out the assumption expressly as they do with other key assumptions and to state in the opinion that they are not taking any position with regard to fairness. In appropriate cases, lawyers also may choose to explain how the courts evaluate fairness. For example, lawyers may explain what are the consequences of a court's determination that a contract is not fair, or they may explain how fairness has both procedural and substantive aspects. If under applicable law validity turns on fairness and a lawyer concludes that a contract is unfair, it would be inappropriate to make a contrary assumption, and the lawyer should decline to give the opinion.

d. Defenses based on misconduct by a party.—A properly created agreement or instrument also may be subject to attack on grounds such as fraud, misrepresentation, duress, violation of fiduciary duties, or breach by the other party. Normally, misconduct by the company will not prevent counsel from opining on the company's obligations because such misconduct normally will not excuse the company's performance. Similarly, misconduct by the opinion recipient normally should not present a problem because the lawyer is entitled to assume without expressly stating it that the recipient has behaved properly and will perform its obligations, express and implied, under the agreement.<sup>96</sup> If, however, the lawyer actually knows of serious misconduct by either party to the transaction, an opinion qualification may well be in order—especially when the lawyer has

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94. DEL. CODE ANN. tit. 8, § 144 (1983). This may be true even when the contract has been approved by disinterested stockholders or directors.

95. In the view of many business lawyers, assumptions of good faith and fair dealing are inherent in all business transactions and to spell them out in a legal opinion is to belabor the obvious.

96. When applicable law would impose unusual or extensive obligations on the opinion recipient by implication and the company's performance would be excused if the opinion recipient failed to perform them, the lawyer should disclose the matter to the recipient. See *K.M.C. Co., Inc. v. Irving Trust Co.*, 757 F.2d 752, 759 (6th Cir. 1985) (holding that a lender had an obligation to give notice before refusing to extend funds under a line of credit even though the agreement did not impose such an obligation expressly. The lawyer ought not to be required, however, to disclose general obligations of a common sense nature such as an obligation to deal in good faith); see also *Cohen v. Ratinoff*, 147 Cal. App. 3d 321, 330, 195 Cal. Rptr. 84, 89 (1983) (holding that where a lease permitted the lessee to assign the lease only with the consent of the lessor, a lessor who refused consent unreasonably violated his duty of good faith and fair dealing and could be held liable for breach of contract).

reason to believe that the opinion will be relied upon by someone other than the parties to the agreement.

e. Other defenses.—Courts also may refuse to enforce agreements and instruments on grounds such as unconscionability,<sup>97</sup> mutual mistake of fact, frustration of purpose, and impossibility of performance or “impracticability.”<sup>98</sup> Because such defenses rest on factual circumstances beyond those that lawyers normally are able or expected to investigate, counsel can give the “legal, valid and binding” opinion unless the agreement is unconscionable on its face or he knows of facts that would clearly excuse the company’s performance.<sup>99</sup>

f. Conflicts with other agreements and instruments.—The “legal, valid and binding” opinion does not cover conflicts between the agreement or instrument and other contractual obligations of the company. Normally, courts will enforce the rights of an innocent party to an agreement or instrument even though the company breached other contractual obligations by entering into or creating it. The standard opinion contains another clause dealing with consistency with other agreements, limited by a “to our knowledge” qualification. Nevertheless, if a lawyer knows that an agreement or instrument violates other contractual obligations of the company, he should not give the opinion, because to do so might aid and abet a tortious interference with a contractual relationship.<sup>100</sup>

97. One commentary sets out the following language for expressly excluding unconscionability problems from the coverage of the opinion:

The opinions expressed in this letter are qualified to the extent that the validity, binding nature, and enforceability of any of the terms of the Loan Documents may be limited or otherwise affected by:

the effect of California law, which provides that a court may refuse to enforce, or may limit the application of, a contract or any clause of a contract which the court finds to have been unconscionable at the time it was made or at the time of enforcement, or an unfair portion of an adhesion contract.

Weise & Duncan, *supra* note 76, at 414, 424. Most lawyers believe that such a qualification is implicit and ordinarily need not be stated expressly.

98. See, e.g., U.C.C. § 2-615 (1978); RESTATEMENT (SECOND) OF CONTRACTS § 261 (1979); E. FARNSWORTH, *supra* note 41, at § 9.6; Prance, *Commercial Impracticability: A Textual and Economic Analysis of Section 2-615 of the Uniform Commercial Code*, 19 IND. L. REV. 457 (1986).

99. See also Wolfson, *supra* note 33, at 98-99 (“Opinion that [the] agreement is binding embodies [the] conclusion that . . . [the] designated party is not precluded from raising defenses of equitable nature (such as agreement being commercially unreasonable), whether such defense would be sustained is within discretion of court.”). Wolfson, however, suggests that the opinion that an agreement is enforceable “embodies [the] conclusion that [the] designated party cannot successfully assert defenses of [an] equitable nature.” *Id.*; cf. TERM LOAN HANDBOOK, *supra* note 3, at 122-23:

The overwhelming majority of opinions make no specific exceptions for some or all of such limitations . . . [C]ounsel appear[s] to rely on there being implied a limitation along the lines, “insofar as contracts generally are legal, valid, binding and enforceable.” However, some of the exceptions commonly taken in legal opinions may limit counsel’s ability to claim that such a limitation (however sensible) must be implied in deciding what the lawyer’s opinion means. The inclusion in every opinion of at least one express qualification of general application . . . puts the implication of the rest in some question.

100. See *supra* note 45.

C. "Enforceable in Accordance with Its Terms" Subject to the Equitable Principles Qualification

The phrase "legal, valid and binding" is frequently followed by the phrase "enforceable in accordance with its terms," modified by an "equitable principles" qualification.<sup>101</sup> This qualification takes various forms. One, added after the word "terms," states "except as may be subject to general principles of equity, regardless of whether such enforceability is considered in a proceeding in equity or at law." Another, added as a separate sentence, states:

Our opinion that the Agreement and the Notes are enforceable each in accordance with their respective terms is subject to the qualifications that . . . the availability of the remedy of specific enforcement, of injunctive relief or of other equitable relief is subject to the discretion of the court before which any proceeding therefor may be brought.

The equitable principles qualification is needed because of the discretionary nature of equitable relief.<sup>102</sup> Without the equitable principles qualification, the enforceability opinion might be taken to confirm that upon a default the other party to the agreement would have an absolute right to an injunction or specific performance. Because the opinion as to enforceability and the equitable principles qualification almost always appear together, they are best analyzed as a single unit. For convenience this Article will refer to them as the "qualified enforceability opinion."

Disagreements over the meaning of legal, valid and binding pale in comparison to the ongoing and heated debate that rages over the meaning of the qualified enforceability opinion. Commentators agree that it means, at the very least, that some remedy would be available—subject to a court's discretion in the case of equitable remedies—for a violation by the company of its obligations. To that extent the phrase has virtually the same meaning as the phrase "legal, valid and binding."<sup>103</sup> The hard question is whether it means anything more.

Many experienced lawyers who have not thought too hard about the question interpret the qualified enforceability opinion as having something to do with specific performance.<sup>104</sup> When pressed, however, they find this view hard to

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101. As discussed below, the qualification may or may not be drafted to qualify the legal, valid and binding opinion as well.

Some lawyers believe the equitable principles qualification is implicit in the opinion and suggest that including it might encourage courts to refuse to enforce the contract as written. See *New York Report*, *supra* note 1, at 1918.

102. Courts have broad discretion to refuse such relief and may do so, for example, because of the difficulty of enforcing the decree. See RESTATEMENT (SECOND) OF CONTRACTS § 366 (1979) ("A promise will not be specifically enforced if the character and magnitude of the performance would impose on the court burdens in enforcement or supervision that are disproportionate to the advantages to be gained from enforcement and to the harm to be suffered from its denial."). Similarly, courts may refuse equitable relief because of unconscionability, plaintiff's unclean hands, or public policy considerations broader than those which would preclude an award of damages. See *id.* § 365, comment.

103. Thus, the opinion also confirms that the agreement or instrument has been "duly authorized, executed and delivered." See *supra* text accompanying note 33.

104. The same view is expressed by a leading lawyer who *has* thought long and hard about the matter. See Fuld I, *supra* note 3, at 930 ("'specifically enforceable,' is a fair interpretation of

defend. The opinion by its terms does not refer to specific performance and is often given about contracts, such as unsecured loan agreements, for which specific performance is not an appropriate remedy. As a result, after discussion and debate, members of the "specific performance" school usually begin looking for a fallback position.

A more subtle view of the qualified enforceability opinion interprets it to mean that the provisions of the agreement that cannot be adequately enforced through an award of money damages are, subject to judicial discretion, eligible for some form of equitable relief.<sup>105</sup> The problem with this modified interpretation is that it places an excessive burden on the opining lawyer, requiring him to analyze each clause to determine its susceptibility to equitable enforcement. When the agreement contains many covenants, only an expert in the arcane complexities of equitable relief could deliver the qualified enforceability opinion without a good deal of research and ratiocination. While the costs of this effort would be substantial, the benefits would not be, because of the uncertainty involved in predicting the availability of equitable relief in any particular case. Opinion recipients do not normally expect such an extensive analysis. If equitable enforcement of a particular provision is of special concern, the opinion recipient can always ask for a specific opinion.<sup>106</sup>

Perhaps because of the difficulty in ascribing meaning to the qualified enforceability opinion, a leading authority has concluded that qualified enforceability adds nothing to "legal, valid and binding" when a bankruptcy exception also is taken.<sup>107</sup> The problem with this conclusion is that it fails to explain why the qualified enforceability opinion is used at all if, after all the qualifiers, it

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the phrase"); Fuld II, *supra* note 3, at 1312; *cf.* Wolfson, *supra* note 33, at 98-99 (stating that "enforceable in accordance with its terms" is probably generally understood to mean that the agreement is specifically enforceable" but expresses the author's own view that "[A] [c]ontract 'enforceable in accordance with its terms' is one court would enforce to provide [the] remedy or relief [the] contract appears on its face to contemplate ('specific performance' or 'specifically enforceable' may be too limiting since remedy or relief contemplated may not be injunctive in nature)."). *But see California Report, supra* note 3, at 1038 (the opinion "does not mean that specific enforcement is available").

Some lawyers omit the phrase "in accordance with its terms" in the belief that the phrase carries the meaning that specific performance would be available. *New York Report, supra* note 1, at 1916. The report states that "there is no meaningful difference between the phrase 'enforceable' and the phrase 'enforceable in accordance with its terms.'" *Id.* The report, however, does not indicate whether they both do or do not cover the availability of specific performance.

105. A lawyer who held this view would decline to give the opinion if, for example, material obligations of the company set forth in the agreement were too indefinite to be enforced in equity. *See Burr v. Greenland*, 356 S.W.2d 370, 373 (Tex. Civ. App. 1962) ("greater certainty respecting the terms and conditions of the contract sought to be enforced is required in equity than at law"). Equitable relief may include not only specific performance, but also an injunction. Thus, a personal service contract may be "enforceable in accordance with its terms" even though the court would not order the performance of the stipulated services, because a court might enjoin performance of the services for anyone else. Nevertheless, when specific performance is vital to the opinion recipient, careful counsel should consider whether to disclose the problem in the opinion if that remedy is unavailable.

106. Sometimes specific performance is of special interest to the opinion recipient. For example, a manufacturer who has sought to assure availability of a key component from a sole source supplier might want to know that he is entitled, subject to judicial discretion, to compel the supplier to deliver that component rather than simply to pay money damages. In that case delivery could be addressed specifically in a separate clause of the opinion.

107. *New York Report, supra* note 1, at 1915.



adds nothing to “legal, valid and binding.” An opinion recipient is likely to believe that the qualified enforceability opinion means something more, and so may a judge.

A fourth view interprets the phrase “enforceable in accordance with its terms,” to mean that a court, subject to equitable principles, would in the event of a default give effect to the provisions, if any, of the agreement relating to enforcement of the parties’ obligations. Such provisions include, for example, arbitration clauses, rights to regain possession of property contributed to a joint venture, liquidated damages provisions, and rights of access to the source code under a software license agreement. In focusing specifically on matters of enforcement, this interpretation fits nicely the wording of the qualified enforceability opinion. The interpretation also serves nicely the needs of the opinion recipient, who can be expected to have a special concern for the enforcement methods he has chosen to include expressly in the agreement.<sup>108</sup> Interpreted this way, the qualified enforceability opinion means something different than the “legal, valid and binding” opinion. “Legal, valid and binding” means only that a court would grant some relief, perhaps only money damages, in the event of a breach, while the qualified enforceability opinion means that a court, “subject to its equitable discretion,” would give effect “as written” to the provisions the parties have agreed upon for enforcing the agreement. Thus, in situations when counsel concludes that an enforcement provision might be given some effect, but is uncertain whether, even apart from general principles of equity, it would be given effect as written, lawyers who think the two opinions mean the same thing would give both opinions while proponents of the fourth view would give “legal, valid and binding” but not the qualified enforceability opinion.<sup>109</sup> This fourth view does not turn on distinctions between law and equity, unsupported by the words of the opinion itself. A corollary of this fourth view, but one that is not always observed in practice, is that the qualified enforceability opinion ought not to be given if the agreement does not contain enforcement provisions.

Another question is whether the equitable principles qualification should modify “legal, valid and binding” as well as “enforceable in accordance with its terms.” Courts have shown an increasing willingness to allow equitable defenses even when the remedy sought is a purely legal one such as damages. This suggests that the safest course is to include an equitable principles qualification even when the opinion does not include the phrase “enforceable in accordance with its terms” and, whether or not that phrase is included, to draft it to qualify “legal, valid and binding” as well.<sup>110</sup>

A final question is how the qualified enforceability opinion should be worded. One leading authority implies that the equitable principles qualification, when it is drafted to refer to “general principles of equity,” covers equitable defenses

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108. This analysis also accords with the practice, at one time generally followed and still followed today by some lawyers, of giving the qualified enforceability opinion only where the agreement or instrument contains express remedies.

109. Alternatively, proponents of the fourth view could give the qualified enforceability opinion but make an exception.

110. For similar reasons the qualification should not be limited, as it sometimes is, to “the enforcement” of the agreement or instrument.

as well as the discretion courts may exercise in granting equitable relief.<sup>111</sup> Equitable defenses include those arising from misrepresentation or duress or violation of public policy, a fiduciary duty or a relationship of trust and confidence. It is not clear whether these defenses are covered by an "equitable principles" qualification that refers only to the discretion exercised by courts in equity and not to general principles of equity.

A form of equitable principles qualification that takes these comments into account would state: "Our opinion that the Agreement [or instrument] is a legal, valid and binding obligation of the Company enforceable in accordance with its terms is subject to . . . general principles of equity, regardless of whether applied in a proceeding in equity or at law."

#### *D. The Bankruptcy Qualification*

As set forth above, the opinion on the status of agreements and instruments is almost always accompanied by a "bankruptcy qualification." A common form of this qualification states, immediately after the phrase "enforceable in accordance with its terms," "except as may be limited by bankruptcy, insolvency or other similar laws affecting the enforcement of creditors' rights in general."<sup>112</sup> Another form states:

Our opinion that the Agreement and the Notes are enforceable each in accordance with their respective terms, is subject to the qualifications that . . . the enforcement of the rights and remedies created thereby is subject to bankruptcy, insolvency, reorganization, moratorium and similar laws of general application affecting the rights and remedies of creditors and secured parties . . . .

Some commentators think a bankruptcy qualification is implicit in the "legal, valid and binding and enforceable in accordance with its terms" opinion or that it is literally unnecessary because bankruptcy proceedings do not render a company's contractual obligations invalid.<sup>113</sup> Nevertheless, bankruptcy proceedings normally result in a severe curtailment of remedies and practicing lawyers include the qualification in their opinions as a matter of course.

Whichever form of bankruptcy qualification is used, the qualification puts the opinion recipient on notice that rights it has bargained for may, if the company encounters financial difficulty, be impaired under laws designed to protect creditors and fix the priority of their claims. In a loan transaction, for example, a noteholder might be unable to collect the full amount of the debt and, in addition, find that its claims are subordinated to those of other creditors under doctrines such as those relating to equitable subordination, preferences, and fraudulent conveyances.

111. *New York Report*, *supra* note 1, at 1918.

112. *Id.* at 1914. The word "similar" is needed to exclude laws such as usury statutes from the coverage of the bankruptcy qualification.

113. *See, e.g., California Report*, *supra* note 3, at 1039; *New York Report*, *supra* note 1, at 1915; *cf. Wolfson*, *supra* note 33, at 101 (stating that the "[m]ere fact bankruptcy laws may preclude payment should not limit opinion as to enforceability (otherwise there should be a 'credit-worthiness' exception).").

The phrase "bankruptcy, insolvency or other similar laws" should adequately alert the opinion recipient to the risks inherent in a company's insolvency. Some lawyers, however, add the terms "reorganization, moratorium or fraudulent conveyance" out of concern that an opinion recipient might not otherwise understand the breadth of the qualification or that a court might not read it so broadly.<sup>114</sup>

When the lawyer knows of a specific problem that is likely to affect the opinion recipient's rights in a material way, he should disclose it in the opinion even if it is covered by the bankruptcy qualification.<sup>115</sup> An example is the fraudulent conveyance problem presented by upstream guaranties<sup>116</sup> and leveraged buyouts.<sup>117</sup> Under the Uniform Fraudulent Conveyance Act, a conveyance made by a business "without fair consideration" is fraudulent if after the conveyance "unreasonably small capital" remains in the business.<sup>118</sup> Conveyances and obligations also are fraudulent if incurred "with actual intent . . . to hinder, delay, or defraud . . . creditors."<sup>119</sup> The Act empowers creditors to set aside fraudulent conveyances under various circumstances, depending on whether the purchaser gave adequate consideration and whether he knew of the fraud.<sup>120</sup> Upstream

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114. See *Weise & Duncan*, *supra* note 76, at 416 n.56 (1985) ("The fraudulent conveyance exception has not been customarily used in the 'bankruptcy' exception. It may not be covered by the 'other similar laws' language in the standard bankruptcy exception since it is not a law that 'generally affects creditors' rights."); *Harter & Klee*, *supra* note 3, at 286 ("[I]f a transaction is set aside under [fraudulent conveyance provisions] . . . those not involving the debtor's insolvency . . . the bankruptcy out should not be interpreted to exclude from the opinion the potential effect of avoidance.").

115. A full discussion of bankruptcy matters may be called for in other situations as well. See *Case & Bernstein*, *supra* note 3, at 12-13:

The necessary depth of treatment [of bankruptcy matters] may depend on how creditworthy the borrower is at the time of closing. For instance, if the opining attorney is delivering an opinion in connection with a short-term unsecured loan to an AAA-rated borrower and the addressee is his own client (with whom he had had frequent bankruptcy discussions), a written bankruptcy analysis may be wholly uncalled for. If the recipient is the "other side," such as a lending institution, and the transaction is the complex, secured financing of a distressed borrower, then a highly detailed bankruptcy analysis may be called for.

Sometimes, discussion between the opining attorney and the intended recipient (and his counsel, if any) can determine how much bankruptcy analysis is needed. More often, the opining attorney will have to make a unilateral, strategic judgment about what level of bankruptcy analysis is appropriate.

*But cf.* Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyers' Association, *An Addendum—Legal Opinions to Third Parties: An Easier Path*, *supra* note 3, at 430 ("it seems appropriate to put the burden on the lender or buyer to specifically require a detailed bankruptcy analysis, to the extent it deems that relevant.").

116. An upstream guaranty is a guaranty by a subsidiary given in support of parent company borrowings.

117. A leveraged buyout is an acquisition in which the credit of the acquired company is used to finance the acquisition. For example, an acquiring company may borrow heavily from a bank to fund its acquisition of the acquired company's stock, and then have the acquired company pay a dividend or some other distribution so that the acquirer can repay the bank. Typically, the dividend or distribution will itself be funded by heavy borrowings by the acquired company. The lawyer may be asked to opine that the acquired company's loan agreement is legal, valid, binding, and enforceable.

118. UNIF. FRAUDULENT CONVEYANCE ACT §5, 7A U.L.A. 504 (1985).

119. *Id.* §7, at 509.

120. UNIF. FRAUDULENT CONVEYANCE ACT §§ 4-9, 7A U.L.A. 474-630 (1918); see UNIF.

guaranties almost always raise the question whether the subsidiary is receiving "fair consideration."<sup>121</sup> Leveraged buyouts often raise the question whether the acquired company is left with "unreasonably small capital" after its assets and credit are used to finance the acquisition.<sup>122</sup> In these circumstances experienced counsel, as a matter of good practice, include in their opinions an express statement concerning the fraudulent conveyance problem.<sup>123</sup>

By way of contrast, many routine transactions—for example a contract for the sale of machinery or equipment in the ordinary course of business by a company in sound financial conditions—present fraudulent conveyance problems only under exceptional circumstances. The bankruptcy qualification permits a lawyer who is not on notice of a fraudulent conveyance problem to give a flat opinion on the purchaser's contractual obligations in such routine transactions without investigating the fairness of the price or the soundness of the purchaser's

FRAUDULENT TRANSFER ACT §§ 1-5, 7A U.L.A. 639-58 (1984). The Bankruptcy Code contains similar provisions applicable to obligations incurred or transfers made within a year prior to the filing of a bankruptcy petition. See 11 U.S.C. § 548 (1982).

121. See *Rubin v. Manufacturers Hanover Trust Co.*, 661 F.2d 979, 993 (2d Cir. 1981) (requiring, for Bankruptcy Act purposes, that consideration be received by each guarantor affiliate); *United States v. Gleneagles Investment Co., Inc.*, 565 F. Supp. 556, 576-77 (M.D. Pa. 1983) (holding, *inter alia*, that guaranties and mortgages, in a leveraged buyout, constituted fraudulent conveyances because they were not given for fair consideration and because the borrowing companies were insolvent after the transaction. The court concluded that acquiring new management that lacked experience in the industry did not constitute fair consideration. In determining solvency, the court looked to the borrowers' corporate group as a whole "[b]ecause the business of the [group] . . . was conducted as though [it] . . . was a single entity and because the [d]efendants urged the court not to look at the solvency of individual . . . members.").

Such arrangements also are vulnerable sometimes to attack as preferences. See 11 U.S.C. § 547(b) (1982).

For general discussions of fraudulent conveyance and equitable subordination questions, see Carl, *Fraudulent Transfer Attacks on Guaranties in Bankruptcy*, 60 AM. BANKR. L.J. 109 (1986); Rosenberg, *Intercorporate Guaranties and the Law of Fraudulent Conveyances: Lender Beware*, 125 U. PA. L. REV. 235 (1976). Corporate power problems presented by guaranties of affiliate borrowings are discussed *supra* text accompanying note 7-9. Curing problems presented by guaranties are discussed *infra* text accompanying note 130-33.

122. Leveraged buyouts also may involve unlawful dividends or other distributions and violations by target management of their fiduciary duties. For a discussion of legal problems raised by leveraged buyouts, see P. BLUMBERG, *supra* note 8, at 200-40, 332-33, 356-57. For a discussion of opinion problems raised by leveraged buyouts, see Schneider, *supra* note 8, at 330-39.

123. In an opinion relating to a guaranty, one approach is to include an express assumption. One version states:

The opinions expressed below, insofar as they relate to the guaranty by the subsidiary of the obligations of the Parent, assume that a court would not find that the Subsidiary, contrary to the determination made by the Board of Directors of the Subsidiary, received less than a reasonably equivalent value in exchange for its guaranty of such obligations outstanding on the date thereof, or subsequently incurred or for any payment made pursuant to such guaranty.

Schneider, *supra* note 8, at 330. Another approach is to give a "reasoned" opinion on the guaranty. Schneider gives an example of a "reasoned" opinion that details the various arguments and authorities under Massachusetts law. *Id.* at 335-36. Schneider observes, "[i]n my view, no lender should want [this] type of opinion because it is a roadmap for a trustee in bankruptcy." *Id.* at 330.

In an opinion on a leveraged buyout, one approach is to state, "[w]e have also assumed that on this date the company is, for all purposes and by any measure, solvent and not left with unreasonably small capital." *Id.* at 337. One authority, however, makes the point that such an approach may be "too elliptical . . . Shouldn't the client be told more specifically what the effects of the assumption are?" Case & Bernstein, *supra* note 3, at 7.

finances, and without qualifying his opinion to cover the possibility that the purchaser's financial condition might deteriorate by the time of performance.

Some forms of bankruptcy qualification, such as the second form quoted above, modify only the "enforceable in accordance with its terms" opinion. It is difficult to see why the qualification should not be drafted to apply to "legal, valid and binding" as well. This would alert opinion recipients that bankruptcy may affect their rights to money damages.<sup>124</sup> The purchaser of a business, for example, should be informed that the bankruptcy of the seller not only could prevent the buyer from compelling the seller to perform its ongoing contractual commitments, but also might deprive him of substantial money damages. Some redrafting of the standard language, therefore, is needed. One formulation would be as follows: "The Agreement [or instrument] is duly authorized, executed and delivered and constitutes a legal, valid and binding obligation of the Company enforceable in accordance with its terms, except as may be limited by bankruptcy, insolvency or similar laws affecting creditors' rights."

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124. Cf. Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyer's Association, *supra* note 3, at 430:

It has been suggested by some lawyers that the bankruptcy exception language should qualify only the word 'enforceable.' Thus, they would rewrite the first sentence of paragraph 4 of the Sample Opinion in the following style: "The Agreement is a legal, valid and binding obligation of the Corporation and, except as may be limited by bankruptcy, insolvency or other similar laws affecting the enforcement of creditors' rights in general, is enforceable against the Corporation in accordance with the terms of the Agreement."

In the view of the members of the Committee there is no meaningful difference between sentence 1 of paragraph 4 and the usage above.

*But see* Case & Bernstein, *supra* note 3, at 3, 5:

It has never been commonly thought that the provisions of prior bankruptcy law affected the validity or legality of any contract terms. Consequently, many lenders and attorneys have considered it unnecessary for [legal, valid and binding] . . . opinions to contain a bankruptcy exception. This is based on the theory that claims remain valid and binding throughout bankruptcy, irrespective of whether they can be enforced. ["Legal, valid and binding"] . . . means only that there has been created some right, some entitlement to a recovery that will be legally recognized (e.g., a claim allowable in bankruptcy or entitled to a money judgment). It does not purport to advise the addressee of what effective remedies there are or when they may be available, once the claim is allowed or judgment is obtained. In other words, [legal, valid and binding] . . . tells the addressee that he will be entitled to legal protection for the bargain but does not purport to say whether the remedy will be award of what was actually bargained for or some other relief, judicially determined to be the legal equivalent of what was bargained for, such as new securities issued in a plan of reorganization.

Many clients do not expect their investments to be invalid in bankruptcy. Most of them know that automatic stays and litigation can delay enforcement, but they expect to have a valid claim on which some kind of distribution will be received (if any is made). If an opinion says generally that validity is subject to bankruptcy, then the client is being told he may well have an invalid or unallowable claim in bankruptcy.

Case and Bernstein, however, go on to list 14 bankruptcy doctrines that might affect the validity as well as the enforceability of a contract clause and state, "[t]his raises the question whether counsel may still always be comfortable in expressing [legal, valid and binding] . . . opinions without taking some specific qualifications relating to the effect of bankruptcy on the validity of particular clauses directly affected by bankruptcy." *Id.* at 6.

Another question concerns the use of the qualifiers "in general" or "of general application" in the bankruptcy qualification. These are best omitted because they might be read to have the undesirable effect of excluding from the qualification bankruptcy-type laws applicable only to one industry, such as the Securities Investor Protection Act.

## II. GIVING THE OPINION

### A. *Supporting the Opinion*

The law of the state of incorporation governs such matters as the company's due organization, its corporate powers, and the procedures it must follow to authorize and execute the agreement or instrument. The law of some other state, often selected in the agreement itself, may govern other aspects of the agreement, in particular its remedy provisions. For matters governed by the law of another jurisdiction, opining lawyers commonly obtain an opinion, formal or informal, from local counsel. When not relying on local counsel, an opining lawyer should take the following steps.

1. To support his "due authorization" opinion, the lawyer should:

a. Satisfy himself that the company was a corporation at all relevant times. Ordinarily this will not be an independent step because the opinion almost invariably includes another clause that expressly covers the corporate status of the company.

b. Obtain and review the agreement or instrument in question, together with any attachments and exhibits. The lawyer should make sure that what he obtains is complete and final and includes all amendments and alterations. In the flurry that surrounds the days before the closing of a major transaction, attachments and exhibits are often left incomplete until the eleventh hour and minor amendments may be agreed upon over the telephone but not promptly reflected in revisions to the working draft. Lawyers satisfy themselves on these points by reviewing an executed copy of the agreement or instrument or by obtaining an officer's certificate confirming that the conformed copy furnished to them is identical to the executed copy.

c. Confirm that the corporation has the corporate power to enter into and perform its obligations under the agreement or instrument. The lawyer will have obtained certified copies of the charter and by-laws to support the corporate status opinion.<sup>125</sup> He should review those documents and the applicable corporate law in order to identify any provisions that would prevent the company from entering into the agreement, creating the instrument, or performing its obligations.

d. Confirm that the agreement or instrument has received the necessary corporate approvals. The lawyers should ascertain whether the charter, by-laws, or applicable corporate statute contain any express requirements for shareholder or director approval. If they do not, the lawyer should look to case law, the nature of the transaction, and the policies and practices of the company in question to determine what approvals are necessary.<sup>126</sup>

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125. FitzGibbon & Glazer, *Legal Opinions on Incorporation*, *supra* note 3.

126. *See supra* text accompanying notes 14-21.

The lawyer should confirm that any necessary resolutions have been duly adopted and remain in full force and effect. The lawyer almost always obtains a secretary's certificate to that effect and may also review the minutes of the meeting or meetings at which the resolutions were adopted—especially if he is company counsel. When the agreement or instrument was approved by a board committee, the lawyer should confirm that the committee had the requisite authority.

Often the resolutions approve the agreement or instrument "in the form presented to the meeting." In such cases, unless counsel was present at the meeting, counsel ordinarily should include a representation in the secretary's certificate that the agreement in the form executed is substantially in the form submitted to the meeting.

e. When the instrument in question is a bond issued under an indenture or an option created under a stock option plan, the lawyer should confirm compliance with the indenture or plan. In the case of a bond indenture, for example, the lawyer should confirm that the bonds have been created in accordance with the procedural requirements of the indenture, such as any requirement of trustee authentication, and that they satisfy any financial tests. Normally, financial requirements are confirmed by a certificate of a company officer or the company's accountants.

2. To confirm that the agreement or instrument has been "duly executed," the lawyer should:

a. Determine which officers have been given the authority to execute the agreement or instrument. Usually the lawyer will rely on a board resolution, but authority to execute agreements and instruments also may be contained in the charter, by-laws, or applicable corporation statute.

b. Determine who holds those offices. Usually the lawyers will obtain a certificate listing the officers and confirming their incumbency. When a lawyer is uneasy about a company's internal procedures, he also may choose to look behind such a certificate and confirm by reviewing the minutes that the officers have been duly elected.

c. Confirm that the agreement or instrument was signed by the proper officers. Lawyers often satisfy themselves with respect to the authenticity of the signatures by observing the signing or, despite misgivings as to their qualifications as handwriting experts, by comparing the signatures on the executed documents with those contained in the incumbency certificate. Alternatively, the lawyer simply may include in his opinion an express assumption with respect to the authenticity of all signatures.<sup>127</sup>

3. To confirm that the agreement or instrument has been "duly delivered," the lawyer often need do no more than attend the closing. Sometimes the agreement or instrument is physically delivered but is "in escrow" pending the

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127. One form of assumption, covering this and related matters, states:

We have assumed the genuineness of all signatures, the authenticity of all documents submitted to us as originals, the conformity to original documents of all documents submitted to us as certified or photostatic copies, and the accuracy and completeness of all corporate records made available to us by the Company and Subsidiaries.

*Massachusetts Sale of Closely-Held Business Report, supra* note 3, at 115 (citation omitted).

transfer of funds or completion of some other closing requirement. The lawyer should confirm that such steps have been completed before releasing the opinion. Sometimes one lawyer holds the documents for both parties and the transaction is closed without physical delivery. When that happens, the lawyer usually can give the "duly delivered" opinion by confirming that the lawyer holding the documents has assumed the role of bailee for the other.

4. To confirm that the agreement or instrument is a "legal, valid and binding obligation of the Company, enforceable in accordance with its terms," the lawyer should:

a. Determine whether the requirements for the formation of a contract have been satisfied. The lawyer should examine the agreement or instrument to confirm that it is not so vague or incomplete that a court would refuse to give it effect and should confirm that consideration requirements have been met.

b. Determine whether any provisions of law or principles of public policy would lead courts to refuse to give effect to the obligations of the company set forth in the agreement or instrument. Depending upon his view of the scope of the enforceability opinion, he also should determine whether a court would give effect to the methods of enforcement set forth in the agreement.

Choice-of-law provisions merit special attention, as do liquidated damages provisions, acceleration clauses, and agreements to submit disputes to arbitration. If the company is in a regulated industry, the regulations and orders of the relevant administrative agency should be considered. When the agreement or instrument requires a filing with an agency, the lawyer should review the provisions establishing the requirement, the documents filed by the company, and any interim or final orders by the agency in response to the filing.

### *B. Handling Defects*

Usually, the easiest and best way to solve an opinion problem, if it is identified early enough, is to cure the defect.<sup>128</sup> Defects in the corporate procedures, by which the agreement or instrument was authorized, can be corrected by obtaining waivers of notice or by holding another meeting. Defects in the execution of the agreement can be cured by arranging for the right persons to sign the agreement. Omissions of key provisions can be cured by adding new language. Terms so vague they might not be enforced, can be sharpened by more precise wording.

Doubts about the legality of a clause often can be resolved by modifying the clause or deleting it from the agreement or instrument. Concerns that a variable interest rate would be usurious above a certain level, for example, usually can be put to rest by adding a ceiling on the rate. Concerns that a stock transfer agreement may be illegal because it unreasonably prohibits transfers, can be alleviated by substituting a right of first refusal—which, as a practical matter, can be drafted to have almost the same effect.<sup>129</sup>

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128. This is consistent with what many lawyers regard as one of the principal purposes of a legal opinion: namely to flush out legal problems.

129. A right of first refusal relating to stock in a closely held company often is tantamount to a flat prohibition on transfer because of the difficulty of getting anyone to enter into serious negotiations when prospective buyers know that someone else—usually the corporation or the other shareholders—can appropriate the fruits of their negotiating labors.



Lawyers sometimes try to cure a questionable provision by adding the savings clause, "to the extent not prohibited by law." Literally, this works, but only by making the opinion about the legality of that provision meaningless. Even when such a qualification is added, many lawyers feel obligated to describe the problem to the opinion recipient.<sup>130</sup>

When a subsidiary's guaranty of a parent company's borrowings constitutes a fraudulent conveyance<sup>131</sup> or exceeds the corporate powers of the subsidiary,<sup>132</sup> the problem sometimes can be resolved by having the lender extend some or all of the loan to the subsidiary<sup>133</sup> or by having the parent agree to extend funds or other benefits to the subsidiary in exchange for the guaranty. In other instances, companies have overcome the problem by merging the subsidiary and the parent prior to the borrowing.

Hard questions arise when a cure can only be achieved in ways the parties regard as unacceptable. In some instances, the opinion recipient may be prepared to live with uncertainty about the legality of a provision on the theory that a right of dubious enforceability is better than none at all. Under these circumstances, the lawyer's job is to ensure that the opinion is technically correct without creating a roadmap for a legal challenge. This can be done by adding a savings clause, by excluding the provision from the coverage of the opinion, by qualifying the opinion, by excluding certain bodies of law from the coverage of the opinion, or by omitting entirely the phrase "legal, valid and binding and enforceable in accordance with its terms." For example, an opinion on an underwriting agreement in a registered public offering typically excludes the indemnification provision. Such an opinion is qualified by reference to public policy

130. See also Case & Bernstein, *supra* note 3, at 16:

. . . [S]ome counsel prefer frequent use of this device, but consider it acceptable only if the qualification language in the agreement is sufficiently specific so that it identifies with particularity the law that could affect validity of the clause. They point out that specific qualifications added on to specific clauses are a much more precise way of informing clients about problems than are vaguely worded "exception" clauses in opinion letters. On the other hand, some lawyers believe that clients' rights should not be impaired by "watering down" agreements to reflect possible adverse interpretations of the law, unless the law is clear and settled that the clause is invalid.

131. See *supra* text accompanying notes 114-23.

132. See *supra* text accompanying notes 5-9.

133. One obvious approach is to dispense with guarantees and have the lender extend several loans, making each member of the corporate group liable only to the extent of the funds it actually receives. This approach only works in the unusual instance when none of the borrowers needs funds in excess of its own creditworthiness.

Another solution may be as follows:

Sometimes . . . problems can be avoided entirely in the parent-subsi- dary context by lending to the subsidiary, rather than to the parent corporation, with a secured "downstream" guaranty running from the parent to the lender. As noted, fair consideration certainly should be found when there is a "downstream" guaranty. In addition, the parent can be required to waive its right of subrogation to the lender's claim against the subsidiary if the parent is called upon to honor its commitment, and the subsidiary can then pass the loan proceeds to the parent, in appropriate circumstances, by way of dividends and loans or repayment of intercompany indebtedness. The net effect of this procedure is precisely the same as if the loan were made to the parent and secured by the assets of the entire group of corporations.

Rosenberg, *supra* note 121, at 263 (citations omitted).

or limitations under the federal securities laws or passes only on due authorization, execution and delivery.

Circumstances may arise, however, when a technical solution to an opinion problem is not enough. When a problem of serious importance to the opinion recipient can be sidestepped by a technical qualification, the lawyer should, as a matter of good practice, make sure the recipient understands the limited nature of the opinion. When the problem is that the transaction violates the law, the lawyer ought not to further the transaction by delivering an opinion, however carefully he has drafted it to avoid addressing the problem.<sup>134</sup>

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134. See *SEC v. National Student Mktg. Corp.*, 457 F. Supp. 682 (D.D.C. 1978).

