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Opinions of Counsel in Corporate Transactions: Opinions on Compliance with the Company's Charter, By-laws, and Contractual Obligations

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INTRODUCTION

The opinion delivered by company counsel at the closing of a corporate transaction typically contains a clause that addresses compliance by the company with its charter, by-laws and contractual obligations. One form of opinion confirms that execution and delivery by the company of the agreement in question and performance by the company of its obligations under the agreement will not conflict with or result in a breach of or default under the company's charter, by-laws or specified contracts. Another form of opinion focuses more broadly on all of the company's activities. This alternative opinion, often requested and often, with good reason, resisted, not only covers the points addressed in the narrower opinion but also confirms that the company is not in violation of its charter or by-laws or in default in the performance of its obligations under contracts to which it is a party or by which it is bound.

This article describes various formulations of the "no-conflicts" opinion, analyzes the scope and meaning of alternative opinion formulations, offers drafting recommendations, and concludes with several suggestions for solving "opinion problems."

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I. THE FORM AND MEANING OF OPINIONS ON COMPLIANCE WITH THE COMPANY'S CHARTER, BY-LAWS AND CONTRACTUAL OBLIGATIONS

A. The Opinion that the Transaction Does Not Violate the Company's Charter, By-laws or Contracts

Ordinarily, company counsel is expected to opine that the steps taken by the company in entering into the agreement and the performance by the company of its obligations under the agreement do not conflict with, breach or result in a violation of the company's charter, by-laws or contractual obligations. In a bank loan, for example, counsel may render an opinion to the lender that:

The execution and delivery of the Agreement and Note [and] the performance by the Corporation of their terms . . . do not conflict with or result in a violation of the Certificate of Incorporation or By-Laws of the Corporation or of any agreement [or] instrument . . . known to us to which the Corporation is a party or is subject.¹

When passing on a corporate transaction, counsel is almost always required to opine that the agreement in question has been "duly authorized, executed and delivered."² Properly interpreted, this phrase confirms, among other things, that the entering into and performance by the company of its obligations under the agreement comply with the company's charter and by-laws.³ Thus, it covers the same ground as the portion of the "no-conflicts" opinion that addresses compliance with other contracts and may require similar qualifications.

No-conflicts language is often included among the representations and warranties of the company in the agreement governing the transaction to which the opinion relates.

¹ New York County Lawyers' Ass'n, a report by the Special Comm. on Legal Opinions in Commercial Transactions, Legal Opinions to Third Parties: An Easier Path, 34 Bus. Law. 1891, 1919 (1979) [hereinafter New York Report]. One published version of the no-conflicts opinion adds the term "other organizational documents" after the reference to the charter and by-laws. Connell, Opinions by Issuer's Counsel in Context of Public Offerings and Related Matters, in Opinions in SEC Transactions 97, 128 (PLI 1988) (quoted at greater length in the Appendix to this Article). This term might be read to include such things as pre-incorporation agreements and stockholder agreements entered into in connection with incorporation. It thus raises many of the concerns lawyers have about the portion of the opinion that passes on compliance with other contracts and may require similar qualifications.

No-conflicts language is often included among the representations and warranties of the company in the agreement governing the transaction to which the opinion relates.


³ Id. at 660.
opinion on the charter and bylaws adds nothing new creates the risk that a court, seeking to avoid a redundant construction, may interpret it more broadly than the standard contracts opinion. This risk, however, should not be overstated; a no-conflicts opinion is generally straightforward and even the most creative judge is unlikely to bend it very far. Thus, while it may be safer to omit the no-conflicts opinion on the charter and by-laws, including it is not terribly risky and, in the face of strong resistance from counsel for the opinion recipient, an opining lawyer may well decide that changing established practice is not worth the battle. Over time, however, as lawyers focus more closely on the relationship between various clauses in the standard opinion, the current practice of rendering an express opinion that the transaction does not conflict with the charter and by-laws could — and probably should — change.

Unlike the portion of the no-conflicts opinion that deals with the company's charter and by-laws, the portion that deals with the company's agreements and instruments adds something new and important to the standard opinion.4 Opinion recipients have good reason to be concerned about the impact of the transaction on the company's other contractual rights and obligations. For example, a lender wants to be sure that its loan will not trigger acceleration, "due on encumbrance," or "cross default" provisions that would require the company to pay off other loans. Similarly, an acquiring company in a merger seeks assurance that the change in control will not result in the automatic termination of a valuable franchise or exclusive dealership.5 Opinion recipients are also concerned about the impact on the transaction of a company's other contractual obligations and, in an extreme case, about their own exposure to liability for inducing breach of contract. In the most famous business lawsuit of the 1980's, Texaco was denied the right to acquire Getty

4 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.

Id. at 685. Accord, A. Field & R. Ryan, Legal Opinions In Corporate Transactions, 6-9 (1988).

5 As discussed infra at xx, the no-conflicts opinion may or may not cover adverse consequences that do not result from an outright breach; it depends on how the opinion is worded. Consequently, if the opinion recipient is concerned about consequences such as termination of a franchise or dealership, it should request a specific opinion clause on the subject.
Oil and was forced into bankruptcy when a court held that by entering into an acquisition agreement with Getty, Texaco had induced Getty to breach its prior acquisition agreement with Pennzoil. Thus, opinion recipients have good reason to request a legal opinion regarding the effect of the transaction on the company’s contractual obligations (and of those obligations on the transaction).

In rendering a “no-conflicts” opinion on a company’s other contracts, counsel should take the following steps:

First, counsel must identify all the applicable agreements and search for relevant provisions. Large companies will likely have numerous agreements, many of which opining counsel has not previously read or even heard about. A search for those agreements could consume weeks of effort and, even then, is unlikely to turn up every applicable agreement, particularly oral agreements and recently-negotiated contracts that have not yet been formalized and placed in the company’s files. Unless the company is newly organized or very small, therefore, counsel will ordinarily want to limit the agreements upon which he opines.

6 See Texaco, Inc. v. Pennzoil Co., 729 S.W.2d 768 (Tex. App.- Houston [1st Dist.] 1987), cert. den. 108 S.Ct. 1305 (1988) (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).

7 “Shareholder agreements, voting trust agreements, loan agreements, agreements... limiting alienation or use of Company assets, settlement agreements... should be reviewed.” Babb, Barnes, Gordon & Kjellenberg, Legal Opinions to Third Parties in Corporate Transactions, 32 Bus. Law. 553, 566 (1977).

An interesting question — but one that will seldom arise in practice — is whether, if the transaction breaches another agreement, the lawyer could disregard the problem on the grounds that the other agreement (or the provision in question) is unenforceable. One leading authority suggests that he or she could:

The Agreements should be read by the opining lawyer as if they were enforceable as written. If a conflict appears from such a reading and the conflicting earlier agreement is governed by the law of another jurisdiction, it might be appropriate to obtain a local counsel’s opinion as to the enforceability of the conflicting provision in the earlier agreement.

New York Report, supra note 1, at 1919 n. 40. Whether this view is correct may depend on how the “no-conflicts” opinion is drafted. If the opinion states that the contract in question does not “conflict” with earlier contracts (rather than using only the technical terms “violate” or “constitute a default under”), a court might conclude that the opinion passes even upon contracts and contractual provisions of dubious enforceability. In any event, as a matter of good practice, a lawyer should normally disclose an important problem under an earlier contract even if he has doubts as to enforceability.

8 In a securities transaction, similar problems may be presented by the portion of the opinion that passes on the adequacy of the disclosure document. In a public offering, for example, counsel sometimes opines that “[t]o the best of counsel’s knowledge and information, there are no contracts, indentures, mortgages, loan agreements,
One common approach is for counsel to state expressly that the opinion covers only agreements "known to us" or "of which we have knowledge." Often, however, this is not a complete solution to the

notes, leases or other instruments required to be described or referred to in the Registration Statement or to be filed as exhibits thereto other than those described or referred to therein or filed or incorporated by reference as exhibits thereto; the descriptions thereof or references thereto are correct in all material respects..." Wolfson, Opinions of Counsel to the Underwriters in Public Offerings of Securities, in Opinion Letters of Counsel 1985 at 65, 139 (P.L.I. 1985)(opinion of issuer's counsel).


One authority suggests that counsel should use the phrase "current actual knowledge" because:

This language more clearly sets forth the intent of the attorney rendering the opinion that the opinion is based only on information that the attorney actually possesses and does not include information that might have been discovered upon further investigation and inquiry. A sample provision that identifies the scope of the lawyer's review and the basis for his knowledge is as follows:

In rendering the opinion set forth in paragraph ___ above based on our current actual knowledge, we have, with your permission, advised you only as to such knowledge as we have obtained from (a) the certificate of ________________ , a copy of which is attached hereto, and our examination of the documents referred to therein; and (b) an interview with officers and responsible employees of Borrower and lawyers presently in our firm whom we have determined are likely, in the ordinary course of their respective duties, to have knowledge of the transactions contemplated by the Loan Documents and the matters covered by this opinion. Except to the extent otherwise set forth above, for purposes of this opinion we have not made an independent review of any contract or agreement that may have been executed by or may now be binding upon Borrower or may affect the Property, nor have we undertaken to review our internal files or any files of Borrower relating to transactions to which Borrower may be a party, or to discuss its transactions or business with any other lawyers in our firm or with any other officers or partners of Borrower.

problem. A law firm must be concerned not only about agreements known to the lawyers working on the transaction but also about agreements unknown to them but known to other members of the firm. Collective bargaining agreements, for example, may have been reviewed only by lawyers in the labor law department; pension agreements by the firm's ERISA lawyers; and leases by lawyers in the real estate department. Counsel may find it exceedingly difficult—and expensive—to communicate the terms of a transaction in sufficient detail to everyone in the firm who has represented a particular client so as to allow them to analyze the impact of the transaction on all the agreements on which they have worked (as well as the impact on the transaction of all those agreements).

A firm must be concerned not only about contracts with respect to which lawyers in the firm have performed substantive legal service, but also about other contracts of which they are aware or might be deemed to be aware. Counsel would almost certainly be held to "know of" the contracts listed in the appendices to the agreement in question or, if the transaction is an underwritten public offering, in the exhibit list contained in Part II of the registration statement filed under the Securities Act of 1933. Counsel might also be held to have knowledge of the contracts listed in the merger agreement or possessed but was not. E.g. Morris v. Reaves, 580 S.W.2d 891, 893 (Ct. Civ. App. Texas 1979) ("[a]ctual knowledge embraces those things of which the one sought to be charged has express information and those things which a reasonably diligent inquiry and exercise of the means of information at hand would have disclosed.").


Unless the lawyer's response indicates otherwise . . . if a law firm or a law department, the auditor may assume that the law firm or department has endeavored, to the extent believed necessary by the firm or department, to determine from lawyers currently in the firm or department who have performed services for the client since the beginning of the fiscal period under audit whether such services involved substantive attention in the form of legal consultation concerning those loss contingencies referred to in Paragraph 5(a) below but, beyond that, no review has been made of any of the client's transactions or other matters for the purpose of identifying loss contingencies to be described in the response.

The Commentary to paragraph 2 states:

[where the auditor's request for information is addressed to a law firm as a firm, the law firm may properly assume that its response is not expected to include any information which may have been communicated to the particular individual by reason of his serving in the capacity of director or officer of the client.

Id. at 1718.

For opinion language that attempts to limit the lawyer's responsibility for knowledge of other lawyers in the firm, see supra note 9.
registration statement for another transaction, possibly even for a transaction in which the firm was not directly involved. For example, an outside law firm that is retained as general counsel for a company after it goes public may be deemed to have knowledge of all the contracts listed as exhibits in the company's initial registration statement even though the firm did not work on those contracts or represent the company in the offering.

Because of these concerns, lawyers frequently supplement the "to our knowledge" qualification with a qualification limiting the contracts covered to those that are material to the company and its business. However, a materiality qualification still leaves counsel with the task of figuring out what "material" means and identifying the material agreements. To keep that task manageable, lawyers often add a further exception, which may take the form of a definition of "material," that rules out large categories of agreements on their face. That exception, for example, may exclude agreements entered into in the ordinary course of business, agreements having a term of less than a specified period (such as one year), and agreements involving less than a specified dollar amount.

Outside law firms representing large companies often argue (not always successfully) that opinion recipients should bear the burden of identifying the agreements on which they want an opinion. Thus, rather than starting with all of a company's agreements and cutting them back with "knowledge" and "materiality" hedges, they suggest

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11 One authority states that a materiality limitation applies even when it is not expressed:

> [A]ny conflicts which are apparent must be material, determined by reference to the effect of such conflict (i) on the other party to the Agreement (e.g. because the conflict creates a material absolute or contingent liability), (ii) on the Company (e.g. because the conflict results in accelerating a material debt obligation), or (iii) in respect of the Agreement (e.g. because the conflict results in a material breach or default under the Agreement).

Babb, Barnes, Gordon & Kjellenberg, supra note 7, at 565. For a discussion of whether a materiality limitation is implicit in the opinion that an agreement or instrument is "legal, valid and binding," see FitzGibbon & Glazer, supra note 2, at 667-68.

12 Cf. A. Field & Ryan, supra note 4, at 6-9 n. 27:

It is inappropriate for a lawyer to rely on a certificate stating that the agreements are the only ones that may bear upon the transaction at hand. Such a certificate would be conclusory in nature. It would prevent the lawyer from judging whether the inquiry was sufficient for giving an opinion on the subject.

13 If the number of agreements remaining after such a limiting provision is small enough, counsel may obtain, and base his opinion on, an officer's certificate listing all of them.
that the opinion pass only on agreements listed in a specially prepared schedule or a list prepared for some other purpose, such as the exhibit list in a Securities Act registration statement or an appendix to a merger agreement. Such listed agreements usually include, among other things, contracts for money borrowed, valuable franchises and distributorships, long-term delivery and supply agreements above a certain dollar value, and long-term leases.\(^\text{14}\)

When outside counsel's opinion is limited to listed agreements, the lawyer for the opinion recipient may be concerned about other agreements of a like nature that are not included on the list. To address that concern, opinion recipients often insist that the opinion be expanded to cover comparable agreements, such as "other agreements relating to money borrowed" or even "any other similar document."\(^\text{15}\) They also often insist that the opinion of outside counsel be supplemented by an unqualified no-conflicts opinion from the company's inside general counsel, who typically will be more familiar with the company's contractual arrangements.

Sometimes lawyers are asked to render an opinion not only on agreements "to which the company is a party" but also on agreements "by which the company is bound" or "to which the company is subject."\(^\text{16}\) Adding these additional phrases may expand the scope of the opinion to include agreements the company has not entered into but as to which it has liability by virtue of an equitable doctrine, such as estoppel or acceptance of benefits.\(^\text{17}\) Under those doc-

\(^{14}\) Lawyers negotiating limitations to the "no conflicts" clause should take care to square the list of agreements on which they are opining with the language in the introductory portions of the opinion identifying the documents counsel has examined. Also, they should conclude the introductory portion of the opinion with the catch-all phrase "such other documents as we considered necessary for purposes of this opinion" or the like.

\(^{15}\) See A. Field & R. Ryan, supra note 4, at 6-8. A longer excerpt from an opinion along these lines quoted by Field and Ryan is contained in the Appendix to this article. An opinion containing such elastic language includes many of the difficulties raised by opinions not limited to specified contracts, and therefore may require the same knowledge and materiality qualifications discussed above. Moreover, before rendering such an opinion, counsel will have to survey lawyers in his firm who might be aware of comparable agreements.

\(^{16}\) An even more drastic expansion of the opinion passes upon contracts "to which any property of the Company is subject." See, e.g., Berkeley, Issues Raised in Request for Legal Opinion for a Public Offering, in Opinions in SEC Transactions 141, 151-52 (P.L.I. 1988).

\(^{17}\) Perhaps that is not the intention: one commentator suggests that this form of words is inserted because the opinion language on conflicts with agreements is often interwoven with language relating to conflicts with laws and the phrase "to which the Company is a party" makes no sense when used to modify "laws." Drafting Legal Opinion Letters 83 (J. Sterba, ed., 1988).
trines, for example, corporations are sometimes bound by pre-incorporation contracts entered into by their promoters. Therefore, unless counsel is willing to assume responsibility for agreements to which the company is not a party, counsel should omit from the opinion the phrases "by which the company is bound" or "to which the company is subject."¹⁸

Second, opining counsel must determine whether the transaction will cause the breach of a relevant agreement. This may entail difficult questions of construction.¹⁹ For example, when a regional underwriter manages an initial public offering for a company, the underwriter often requires the company to grant it a right of first refusal on future transactions of a similar nature.²⁰ If the company prospers and later seeks to broaden its investor base through a nationwide offering of securities, the lawyer may have to determine whether the proposed offering is a "transaction of a similar nature," requiring the company to extend to the regional firm, despite its lack of national distribution capacity, the opportunity to serve as managing underwriter.²¹ Similarly, counsel for a distributor may have to worry about the construction of a barebones exclusive distributorship agreement when rendering an opinion in connection with the distributor's acquisition of another distributor.²²

The lawyer's task is greatly complicated when he is called upon to construe an agreement governed by the law of a state in which he is not admitted to practice. Although opinions ordinarily state that counsel is only passing upon the laws of a specified jurisdiction or jurisdictions, counsel may well have an obligation, when faced with a hard question of construction of a contract governed by another state’s law, to point out the problem in the opinion or to resolve it by consulting with local counsel.²³

¹⁸ The phrases "by which the company is bound" or "to which the company is subject" may also be intended to refer solely to contracts of predecessor corporations. If this is true, then the opinion should be drafted so as to make that intention clear.

¹⁹ One authority states that the no-conflicts opinion relates only to "clear and present (or inevitable) conflicts," apparently meaning that the lawyer does not have to worry about conflicts that are only arguable. Babb, Barnes, Gordon & Kjellenberg, supra note 7, at 565. Nothing in the language or purposes of the standard opinion supports that view.

²⁰ Clauses conferring such rights often do not go into much detail.

²¹ Often the uncertainty inherent in the term "similar" leads to a compromise in which a national firm becomes lead underwriter and the regional firm a co-manager.


²³ One important authority states: The litigation and lack of conflict with other agreements opinions are ones that lawyers give as if they did not involve the law of many states. Yet we
When the requirements of earlier agreements are complex and include financial covenants, determining whether the transaction will breach any of those covenants may require a financial analysis that is well beyond counsel's expertise. For example, a long-term loan agreement may contain a covenant prohibiting a company from effecting further borrowings unless certain financial tests are satisfied. Those tests in turn may require an analysis of the company's overall indebtedness as well as borrowings under its other credit agreements and may entail complex mathematical calculations. Some commentators, probably out of concern for the burdens such tasks may impose on the lawyer, take the view that the opinion relates only to conflicts that are apparent on their face:

This opinion addresses itself to clear and present (or inevitable) conflicts which are ascertainable from the face of the Agreement, *vis a vis* . . . third-party agreement[s] . . . . It does not . . . require Counsel to determine the aggregate effect of outstanding agreements under financial ratios or aggregate dollar exceptions to financial covenants.24

As attractive as this view may be from the standpoint of opining counsel, it does not square with the language of the opinion, which gives no hint of any such exception. Perhaps even more important, it ignores the very purpose of the opinion, which is to provide the opinion recipient with assurance that the transaction will not breach, or result in a default under, a company's key agreements. Thus, disregarding financial covenants, without expressly saying so in the opinion, may be risky for opining counsel. The better — and safer — practice is for counsel to rely on certificates of the company's financial officers or outside auditors for matters pertaining to compliance with financial covenants.

*Third*, the portion of the opinion that confirms that the "performance by the company of its obligations" under the agreement in question will not violate the company's other agreements requires counsel to consider not only the obligations the company must perform at and prior to the closing, but also the obligations it is required to perform in the future.25 Some obligations, such as the re-

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25 New York Report 1920-21. This report distinguishes between "performance" and

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A. Field & Ryan, *supra* note 4, at sec. 3.05[5].

Lawyers give these opinions as experts in reading legal documents rather than lawyers in particular jurisdictions. The practice limitation does not apply to those opinions, which are more in the nature of a documentary review than an opinion.
requirement in a loan agreement that the company pay interest and repay principal, are obvious. Others, however, are less obvious. A financing agreement may contain covenants requiring the company to maintain inventories at a particular plant and to supply the lender periodically with information about the company's financial condition. Although such covenants ordinarily pose no problem, they may require that counsel add an opinion qualification under certain circumstances. For example, if the plant is leased and the inventories include volatile chemicals, maintenance of those chemicals at the plant may violate a provision of the lease relating to storage of hazardous substances. Similarly, if the financial information the company is required to provide includes a breakdown of sales to major customers, disclosure of that information may violate an agreement with a key customer requiring that the dollar value of its purchases be kept confidential. To take another example, a stock purchase contract permitting preferred stockholders to elect a majority of the board of directors following a default in the payment of dividends could conflict with change-in-control provisions in a company's loan agreements, leases or franchise agreements. Because of such concerns, counsel may seek to limit the opinion by substituting for the word "performance" a phrase, such as the "payment of the indebtedness represented by the Note," that identifies precisely the future obligations on which counsel is opining.

A further problem arises when performance of the company's obligations under the agreement in question may or may not violate one of the company's other agreements, depending on the circumstances at the time of performance. For example, if the company is a party to a loan agreement containing a covenant that requires it to maintain a specified net worth and it subsequently enters into an agreement to issue redeemable preferred stock, the later redemption of that stock could result in a breach of the net worth covenant depending upon the company's financial performance during the interim period. When the "no conflicts" opinion speaks in the present tense, as is customary, it does not literally cover such problems. But as a matter of good practice, lawyers may choose to disclose such "contingent violations" to opinion recipients if they regard a violation as likely to occur and the consequences as especially significant.

Fourth, counsel may have to consider whether the opinion covers adverse consequences that do not technically constitute a violation or breach of a company's other agreements but that have a similar
effect on the company. For example, as a result of an initial public offering, a company may be required to discharge industrial revenue bonds or to redeem preferred stock or, as a result of a merger, company officers may become entitled to exercise golden parachute rights and lessors may gain the right to raise the rent. In each case, the transaction may not "violate" or "breach" the other agreements, but the effect is equally detrimental to the company. Although such consequences are no doubt of interest to the opinion recipient, an opinion that uses only the technical terms "violation," "breach" and "default" should not be interpreted to cover them. Opinions are precisely worded documents, and technical terms should not be read to have more than their generally understood meanings. If an opinion recipient wants more, he (or his counsel) should bear the burden of asking for it.

Many opinions confirm not only that there is no "violation," "breach" or "default," but also that the agreement in question will not "conflict" with a company's other agreements. Unlike those other terms, "conflict" is not a technical word and thus is susceptible to a less technical reading. Under some circumstances, it is conceivable that a judge could interpret "conflict" to encompass adverse consequences comparable to those resulting from a violation or breach. Such consequences could, for example, include repayment of low-interest indebtedness or redemption of low-cost preferred stock. Counsel wishing to avoid this risk should limit use of the word "conflict" to the charter and by-laws, where the terms "breach," "violation," or "default" are not suitable. Even with this limitation, however, counsel should remain sensitive to any major adverse consequences arising under other agreements. As a matter of good practice, lawyers often disclose such consequences in connection with their no-conflicts opinions.

Sometimes opining counsel is asked to add to a no-conflicts opinion a statement that the transaction in question will not "result in the creation or imposition of any [lien upon any of the property or assets] of the company." This opinion is intended to assure the opinion recipient that the transaction will not trigger a provision in one of the company's other agreements that might convey to a creditor a security interest in the company's property. This is one of the adverse consequences that may not be covered by the opinion dealing with violations, breaches or defaults and may be a matter of le-

26 See, e.g., Wander, Goldstein & Rose, Issues in Legal Opinions 17 (Paper prepared for the Eighth Annual Southern Securities Institute, Miami, Florida, Feb. 18-19, 1988). (Sometimes such opinions state, more broadly, that the transaction will not "result in or permit the imposition of any lien, charge or encumbrance").
The Company is not, nor with the giving of notice or lapse of time or both would be, in violation of or in default under, nor will the execution or delivery of the Underwriting Agreement or consummation of the transactions contemplated thereby result in a violation of or constitute a default under, the Articles of Incorporation or By-laws, or any agreement, indenture, or other instrument known to such counsel, to which the Company is a party or by which it may be bound, or to which any property of the Company is subject . . . .

Experienced counsel usually refuse to render this opinion because it would require a detailed factual investigation into all of the company’s business activities. Counsel would have to consider, for example, whether any of the company’s charitable contributions, guarantees of affiliate debts or loans to shareholders exceeded the corporate powers provisions of the charter. In addition, counsel would have to ascertain that all of the company’s contractual obligations had been complied with, including, for example, the timely payment of its rent and the conformity of its goods with contractual specifications. These matters lie largely outside the lawyer’s competence. Even when qualifications are added, as they sometimes are, relating to materiality or the lawyer’s knowledge or limiting the

opinion to listed agreements or agreements "relating to money bor-
rowed," the lawyer is still not qualified to opine on these matters. Opinion recipients should satisfy their needs in this area through representations by the company and officers' certificates.

II. HANDLING DEFECTS

When counsel discovers that the transaction creates a significant violation of one of the company's contractual obligations, the parties will probably insist that the violation be cured. A waiver or amend-
ment to the contract can often cure contractual problems. For exam-
ple, the lender under a long-term financing arrangement may agree to waive restrictions on further borrowings, at least as they relate to the transaction in question. A shareholder may waive contractual preemptive rights to facilitate a stock offering he believes to be in the company's and his best interest. Alternatively, the stockholder may agree to amend his contractual preemptive rights to carve out certain types of stock offerings, such as sales to venture capital firms.

When the other party to the contract refuses to waive its rights or when the company wishes, for reasons of confidentiality, to avoid requesting a waiver, another approach may be to terminate the third party's rights. This termination may be effected by paying off a loan, invoking a termination clause, or, in the case of contractual preemptive rights, exercising a right to repurchase the shares.

A final, and sometimes the only practical, solution is to alert the opinion recipient to the problem (which in fact is the opinion's prin-
cipal purpose) and to take an express exception in the opinion.
Appendix

The following passages have been taken from the portions of various published legal opinions dealing with compliance with the charter, by-laws and contracts. They are not presented as models; many of them contain language the authors do not recommend.

I. OPINION LANGUAGE CONFIRMING COMPLIANCE BY THE TRANSACTION IN QUESTION WITH THE CHARTER, BY-LAWS AND CONTRACTS


The execution and delivery of the agreement and the performance by the Company of its terms do not conflict with or result in a violation of the Company's articles of incorporation or bylaws . . . and, to our knowledge, do not conflict with and will not constitute a material breach of the terms, conditions or provisions of or constitute a default under any material contract, undertaking, indenture or other agreement or instrument by which the Company is bound or to which it is a party.

REPORT OF THE STATE BAR OF ARIZONA CORPORATE, BANKING, AND BUSINESS LAW SECTION SUBCOMMITTEE ON RENDERING LEGAL OPINIONS IN BUSINESS TRANSACTIONS 27 (February 1, 1989):

The execution and delivery of the Documents and consummation of the Transaction by the Company will not conflict with or result in a violation of the Company's Articles of Incorporation or bylaws. . . .

* * *

Based solely upon [our knowledge] [and a review of those agreements disclosed to us by the Company on the [attached] officer's certificate dated , 19 ] the execution and delivery of the Documents and consummation of the Transaction by the Company will not conflict with or result in a violation of any contract, indenture, instrument, or other agreement to which the Company is a party or by which it is bound.

The execution, delivery and performance of and compliance with the terms of the Agreement, and the issuance of the Shares (and the Common issuable upon conversion thereof), do not violate any provision of the Restated Articles of Incorporation or Bylaws. To our knowledge, the execution, delivery and performance of and compliance with the Agreement, and the issuance of the Shares (and the Common issuable upon Conversion thereof) have not resulted and will not result in any violation of, or conflict with, or constitute a default under, any material contract, agreement, instrument, judgment or decree binding upon the Company.

Connell, Opinions by Issuer’s Counsel in Context of Public Offerings and Related Matters, in OPINIONS IN SEC TRANSACTIONS 97, 128-29 (P.L.I. 1988):

Neither the offer, sale or delivery of the Shares, the execution, delivery or performance of this Agreement, compliance by the Company with all provisions hereof nor consummation by the Company of the transactions contemplated hereby conflicts or will conflict with or constitutes or will constitute a breach of, or a default under, the certificate or articles of incorporation or bylaws, or other organizational documents, of the Company or any of the Susidiaries or any agreement, indenture, lease or other instrument to which the Company or any of the Subsidiaries is a party or by which any of their respective properties is bound [that is made an exhibit to the Registration Statement], or is known to such counsel after reasonable inquiry, or will result in the creation or imposition of any lien, charge or encumbrance upon any property or assets of the Company or any of the Subsidiaries.


The execution and delivery of the Agreement and Note [and] the performance by the Corporation of their terms do not conflict with or result in a violation of the Certificate of Incorporation or By-Laws of the Corporation or of any agreement [or] instrument known to us to which the Corporation is a party or is subject.

A. Field & R. Ryan, Legal Opinions In Corporate Transactions (1988)(Form 1-3 paragraph 2):

The execution, delivery and performance by the Borrower of the
Credit Agreement and the Notes do not contravene (i) the Charter or the By-laws or . . . (iii) any contractual or legal restriction contained in any document listed in the Certificate or, to the best of our knowledge, contained in any other similar document.


The Agreement does not conflict with the Company’s Articles of Incorporation or by-laws or with any agreements . . . known to us . . . .

The execution and delivery of the Agreement and the consummation of the transactions provided or contemplated in the Agreement and compliance with the terms of the Agreement . . . will not conflict with, or result in a breach of, or constitute a default or grounds of acceleration under, or violate . . . any provision of any indenture, mortgage, deed of trust, loan agreement, lease, financing agreement, bond, debenture . . . any agreement [etc.] to which the company is a party or by which it may be bound or to which any of the Company’s property or assets is subject . . . .

Joint Committee of the Real Property Section of the State Bar of California and the Real Property Section of the Los Angeles County Bar Association, *Legal Opinions in California Real Estate Transactions*, 42 Bus. Law. 1139, 1188 (1987):

To our current actual knowledge, neither the execution and delivery of the Loan Documents nor the payment of the indebtedness evidenced by the Note will conflict with or result in a material breach by Borrower of or constitute an Event of Default under any contract, indenture, instrument, or other agreement (i) by which Borrower is bound or to which it is now a party, or (ii) which creates a lien on or security interest in the Real Property or the Personal Property.


The execution, delivery and performance of the Agreement and the Other Agreements, the issuance of the Shares, Debentures, Conver-
sion Shares and Notes the consummation of the transactions described in the Registration Statement and Prospectuses contemplated by the Agreement and by the Other Agreements and compliance with the terms thereof will not result in a breach of or conflict with or constitute a default (or an event which with notice or lapse of time, or both, would constitute a default) under, or result in the creation or imposition of any lien, charge or encumbrance upon any of the property or assets of the Company or any of its Subsidiaries pursuant to the terms of, any indenture, mortgage, deed of trust, loan agreement, note, lease or other agreement or instrument known to us to which the Company or any of its Subsidiaries is a party or to which they or their properties are subject.


To the best of counsel's knowledge and information, the execution and delivery of the Purchase Agreement and the consummation of the transactions contemplated in the Purchase Agreement will not conflict with or constitute a material breach of, or default under, the charter or by-laws of the Company or any contract, indenture, mortgage loan agreement, note, lease or other instrument to which the Company of its subsidiaries is a party or by which it or any of them may be bound that is material to the Company and its subsidiaries considered as one enterprise.

II. OPINION LANGUAGE CONFIRMING COMPLIANCE BY THE COMPANY WITH THE CHARTER, BY-LAWS AND CONTRACTS


Except as set forth in the Agreement, the Company is not in violation of any term of its Restated Articles of Incorporation or Bylaws, or, to our knowledge, in any material respect of any term or provision of any material contract, agreement, instrument, judgment or decree binding upon the Company.


However, it is noteworthy that the opinion language mentioned in the documents is subject to the standards and requirements of the securities laws and regulations.
To the best of counsel's knowledge and information, there are no contracts, indentures, mortgages, loan agreements, notes, leases or other instruments required to be described or referred to in the Registration Statement or to be filed as exhibits thereto other than those described or referred to therein or filed or incorporated by reference as exhibits thereto; the descriptions thereof or references thereto are correct in all material respects; and no default exists in any material respect in the due performance or observance of any obligation, agreement, covenant or condition contained in any contract, indenture, loan agreement, note or lease so described, referred to, filed or incorporated by reference.


The Company is not, nor with the giving of notice or lapse of time or both would be, in violation of or in default under, nor will the execution or delivery of the Underwriting Agreement or consummation of the transactions contemplated thereby result in a violation of or constitute a default under, the Articles of Incorporation or By-laws, or any agreement, indenture, or other instrument known to such counsel, to which the Company is a party or by which it may be bound, or to which any property of the Company is subject, nor will the performance by the Company of its obligations under the Underwriting Agreement . . . to the knowledge of such counsel result in the creation or imposition of any lien, charge, claim or encumbrance upon any property or asset of the Company.


The Company is not in violation of its charter or bylaws and, to the best of our knowledge, no default exists (and no event has occurred which with notice or lapse of time, or both, would constitute a default) in the due performance and observance of any term, covenant or condition of any indenture, mortgage, deed of trust, loan agreement, note, lease or other agreement or instrument known to us to which the Company or any of its Subsidiaries is a party to which they or their properties are subject where such default could have a material adverse effect on the business or financial condition of the Company and its Subsidiaries, taken as a whole.