

REAL ESTATE FINANCE SUBSECTION

THE ISSUANCE OF UCC OPINIONS IN CONNECTION WITH THE ORIGINATION OF LOANS SECURED PRIMARILY BY REAL ESTATE

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MAY 19, 2004

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I. **INTRODUCTION:** This program will focus on the issuance of UCC Opinions in connection with loans secured primarily by real estate and which include personal property as additional collateral. This program is not intended to cover the issuance of UCC Opinions where personal property is intended to be the primary source of collateral.

II. **PURPOSE OF THE OPINION LETTER**

- A. **Generally.** Attorneys generally approach the issuance of opinion letters in connection with real estate secured loans in one of two ways. In the typical case, the opinion letter is a required closing delivery and is expected to force the borrower's attorney that renders the opinion to undertake the necessary due diligence to insure that the borrower has the authority to enter into the loan transaction and execute the loan documents; the opinion letter also serves to disclose to the lender any enforceability issues of which they should be aware. In this first case, the opinion letter is considered to be a tool to flush out and disclose issues, but is not intended to make the opinion letter issuer a guarantor of the opinions being given. In some cases, however, not only does the opinion letter serve the purposes described above, it may also be viewed as a vehicle to provide the lender with a "guarantee" with respect to the opinions being given. This issue typically manifests itself in terms of the assumptions and qualifications that the opinion giver is permitted to include in its opinion.
- B. **Authority.** All opinions generally include an "authority opinion" in order to confirm that the borrower has the authority and capacity to enter into the loan transaction and to execute the documents evidencing and securing the loan. The rendering of this opinion requires the borrower's counsel to review, and be familiar with, the borrower's (and its constituent partners and members) organizational documents.
- C. **Enforceability.** This part of the opinion (often times also referred to as the "remedies" opinion) typically provides that the loan documents are "valid, binding and enforceable" against the borrower, subject to various qualifications and based upon certain assumptions. This is typically considered the most important part of the opinion to the lender since it advises the lender that its documents should be upheld if they are litigated, subject to the stated qualifications. The enforceability opinion is not intended to, and is not generally understood to, express any opinion regarding the creation, perfection or priority of personal property security interests that may be created under the loan documents. Those opinions, if given, are covered through the rendering of the "security interest" opinion.
- D. **The Security Interest Opinion.** As set forth below, the "security interest opinion" potentially covers three different areas, attachment, perfection and

priority. All three of these areas are specifically covered in the California Uniform Commercial Code (the “UCC”) and have been, and will continue to be, the object of a great deal of debate in connection with the issuance of the security interest opinion.

(i) **Attachment:** In accordance with the provisions of Section 9203 of the UCC, “a security interest attaches to collateral when it becomes enforceable against the debtor with respect to the collateral, unless an agreement expressly postpones the times of attachment.” Subject to certain exceptions, in accordance with the provisions of Section 9203(b) of the UCC, generally, a security interest is enforceable against the debtor and third parties with respect to personal property collateral only if value has been given, the debtor has rights in the collateral (or the power to transfer rights to the secured party) and the debtor has authenticated a security agreement that provides a sufficient description of the collateral. Typically, the opinion giver either assumes the existence of the attachment requirements or indicates that its opinion does not cover them since they are factual in nature. An obviously, but important, question to consider is the State law that will apply with respect to the creation of the security interest.

(ii) **Perfection:** Generally, perfection of a security interest in personal property covered by Article 9 of the UCC means that those steps required to afford the secured party protection under the UCC against the claims of third parties have been taken. The method of perfection for various forms of personal property vary and are each expressly covered by various provisions of the UCC. The typical methods of perfecting include perfection by filing a financing statement, perfection through possession or delivery and perfection through control. Similar to addressing the “attachment” issue, the threshold question to be addressed in connection with the granting of a perfection opinion is the State law that shall apply with respect to the perfection of a specific type of personal property, since there are specific choice of law provisions set forth in the UCC that must be followed. The opinion giver will generally assume the existence of many of the elements necessary to satisfy the requirements for perfection.

(iii) **Priority:** The priority opinion provides the opinion recipient with an opinion concerning the ranking of its personal property security interest as against other third parties that may also hold a security interest in the personal property collateral. This opinion is virtually never given and, in fact, most opinions typically expressly provide that no opinion regarding priority is being rendered.

III. TREATMENT OF THE PERSONAL PROPERTY OPINION IN OPINION REPORTS

A. Identification of Reports

- (i) California Security Interest Opinion Report – Report Regarding Legal Opinions in Personal Property Secured Transactions – Uniform

Commercial Code Committee of the Business Law Section of the State Bar of California – December, 1988 (“California Report”)

- (ii) Tri-Bar Report – Special Report of the TriBar Opinion Committee: U.C.C. Security Interest Opinions – Revised Article 9, 58 Business Lawyer 1452 (2003)
- (iii) Pending Report of the Uniform Commercial Code Committee of the Business Law Section of the State Bar of California – scheduled for publication in September 2004; it is in response to the TriBar Report and would replace the California Report

- B. Opinions generally given
- C. Personal property routinely covered
- D. Personal property not routinely covered

IV. POTENTIAL IMPACT ON THE HISTORICAL CONTENT OF THE SECURITY INTEREST OPINION CAUSED BY REVISED ARTICLE 9

- A. Documentation for Transactions
 - 1. Documentation historically used
 - 2. New documentation and review
- B. Assumptions
- C. Opinions (see V below)
- D. Qualifications

V. CURRENT RECOMMENDATIONS REGARDING CONTENT OF THE OPINIONS GIVEN IN THE SECURITY INTEREST OPINION LETTER

- A. Creation or attachment of the security interest, including choice of law
- B. Perfection, including choice of law
 - 1. Choice of law
 - (a) Non-possessory vs. possessory security interests
 - (b) Deposit Accounts
 - 2. Requirements for Perfection Opinion
 - (a) Required “attachment” of security interest
 - (b) Successful Method of Perfection (filing, possession, control)

- C. Priority
 - 1. Analysis in the California Report
 - 2. Analysis in the TriBar Report
- D. Opinions on Certificated Securities, Security Entitlements and Securities Accounts
- E. Real benefits, if any, to rendering of personal property opinion
- F. Forms of Opinion Letters
 - 1. Exhibit A to the TriBar Report
 - 2. Other

VI. EAGLE 9 UCC INSURANCE AS AN ALTERNATIVE OR SUBSTITUTE TO OPINION LETTERS

- A. What it covers/offers
 - (i) Validity/enforceability of personal property security interest
 - (ii) Perfection failures
 - (iii) Priority
 - (iv) Fraud, forgery, undue influence, incompetency, lack of authority
 - (v) Certain bankruptcy coverages
 - (vi) Defense and indemnity
- B. What it does not cover
 - (i) Ownership of pledged collateral
 - (ii) Specific UCC Policy Exclusions
 - (iii) Other Exclusions similar to ALTA Real Estate Loan Policy
- C. Recommendations regarding its usage

VII. CONCLUSIONS AND RECOMMENDATIONS