CURRENT DEVELOPMENTS: LAWYERS' OPINIONS IN BANKING TRANSACTIONS

TOM POULTON

Arthur Robinson & Hedderwicks
Solicitors, Melbourne

It was interesting that Suzanne Corcoran said that she feels that there is a meaning for good standing in Australia. It is certainly an expression which my own firm tries to keep out of opinions. My partner Tony Browne still claims to this day having seen an opinion which said that the managing director of the borrower was a member of the Royal Melbourne Golf Club and the Australian Club and yes, the company is in very good standing. I think that is all it means in Australia, personally.

I will lead you through some aspects of opinions. I hope you can draw the strands together, because it is a little bit random. The first one is really the inter-relationship of the opinion and the borrower's warranties. You will be well aware of the close parallels between the borrower's representations and warranties in the credit agreement and the contents of the legal opinion. One really forms the basis for the other and it is usually the warranties which are negotiated first. The main area of difference is likely to be that the representations and warranties are likely also to cover questions of fact which are inappropriate matters for inclusion in the legal opinion. The converse, perhaps surprisingly, is not true. Lenders' lawyers have for so long insisted on borrowers representing and warranting as to legal conclusions that it would be a brave lawyer indeed who decided to omit them from the credit agreement and rely instead on the legal opinion in this regard.

There will be occasions where the lender will insist that the borrower's legal opinion also extends to certain questions of fact, or mixed fact and law - for example, that the borrower's issued shares are held by certain entities in certain proportions, where shareholding is an important element to the transaction.

My own view is that the borrower's lawyer should be very careful in agreeing to opine as to issues of fact, particularly where those issues of fact are incapable of direct verification by the lawyer. In particular, if the lawyer can only give his opinion as to a particular matter on the basis of the certificate of his

own client, the borrower, there seems to be no point at all in including that matter in the opinion. If it is included, the lawyer might well be thought to be underwriting the client's representations and warranties, and this is where Suzanne was saying that as a lawyer you have an obligation to check what your client is saying. You might get a certificate, but a good lawyer will not ask his client to sign something which he would not be prepared himself to sign - he should not just throw the onus on the client.

When negotiating the representations and warranties it is in my view incumbent on the borrower's lawyer to show the same enthusiasm in protecting his client as he shows when negotiating the equivalent provisions in his own opinion. Otherwise he might find himself hoist on his own petard. It is very difficult to justify as a general matter accepting one form of words in the credit agreement while insisting on another formulation in the opinion. I know that lenders' lawyers have long argued that it is unnecessary for a borrower to take the same exceptions, to make the same qualifications to its representations and warranties, as its lawyer will in the legal opinion. I personally have a great deal of difficulty with this. I do not like my client signing things which I would not be prepared to sign. My own experience in recent times has been that lenders' lawyers have become a little bit more condescending in this regard and they are prepared to accept incorporation of exceptions and qualifications by reference to the opinion itself. So you will have some sort of sentence to the effect of "Subject to the matters set forth in paragraphs (a) to (j) of Appendix X hereto ... ."

The next aspect that I would like to deal with is very close to my heart and that is the matter of qualifications. I think that opinions are often read by lenders' lawyers more for the qualifications than for the substance of the opinion itself. I believe they expect to have an informative time reading the qualifications and they would expect that the qualifications would disclose the things of which they ought to be aware before committing their client to lending the money. On the other hand I accept Suzanne's statement that Australian lawyers often pick up a whole lot of qualifications which I am not sure are reasonably necessary.

The extent of qualifications seems of late to have become a more fertile ground for discussion between lenders and borrowers. I may be mistaken, but my own impression these days is that lenders are increasingly anxious to reduce the size of the legal opinion, or rather the qualifications, while the opinion itself tends to get longer.

One of the major concerns faced by a borrower's lawyer when deciding whether or not to include a qualification is simply where to draw the line. Some qualifications are clearly necessary. Others, while arguable, may not advance the sum total

of human knowledge very far. The problem with taking the latter qualifications is that the lawyer may be increasing, rather than reducing, his exposure. In particular, he may be subsequently faced with the argument that since you took such and such a qualification, which deals with a fairly remote contingency, we, the lenders, are entitled to assume that you have drawn every possibility to our attention.

While different lawyers may have different views, I am inclined to categorise the following qualifications as "necessary". The first is that enforcement may be limited or affected by the general rules and laws relating to bankruptcy, insolvency, liquidation, reorganisation or reconstruction and other rules and laws of general application affecting the rights and remedies of creditors. This is particularly important if, as Suzanne was saying, the opinion itself talks about enforceability in accordance with its terms, because, when events of insolvency strike, the rights of creditors are very quickly rearranged by matters well beyond their control.

The second qualification is that a reference to the legality, validity and binding effect of an obligation or to its enforceability is not to be taken as indicating enforceability thereof by way of specific performance, injunctive relief or any other discretionary remedy. This also tends to go to enforceability in accordance with the agreement's terms. If a bank thinks that it can get specific performance of the obligation to deliver financial statements, it is better that it should not be allowed to do so.

The third necessary qualification is that all instruments the subject of the opinion constitute the legal, valid and binding obligations of the intended obligor under or by virtue of the respective laws (other than your own laws) by and in accordance with which the same are governed, and that to the extent that performance is to take place outside your own jurisdiction such performance is not illegal in the place or places where performance is required. Australian courts are unlikely to enforce an obligation which is illegal in the jurisdiction where it is to be performed.

The fourth necessary qualification is that nothing in the opinion is to be taken as indicating that a judgment for a monetary amount will be given in the courts of Victoria in any currency other than Australian currency. The Miliangos principle has not yet been accepted in Victoria according to my understanding. I believe it has been accepted in New South Wales in a 1984 case (Maschinenfabrik Augsburg-Nurenburg AG v. Altikar Pty Ltd [1984] 3 NSWLR 152) and it may be that the true position in Victoria is that it will now be given effect to there.

The fifth qualification is that a provision for the payment of interest at an increased rate after default may be treated as being in the nature of a penalty, in which event the courts of

your own State may decline to enforce the provision - this does not require much explanation.

The sixth qualification which seems to be peculiarly Australian and sticks its head up in secured transactions is that by reason of section 261 of the Income Tax Assessment Act 1936 the undertaking of the borrower to pay or bear any amount of withholding tax or to pay any additional amount in respect of withholding tax may be void. Lawyers have become so scared of this that I have even had it put to me that this qualification should be included in an opinion in relation to a transaction which is secured only by guarantee. I have some difficulty with that myself. But people seem to be very careful to protect their backsides.

Additional qualifications are often taken, but their necessity seems to me to be much more debatable. The first one relates to limitation of actions and set-off and counter-claim. My own view is that a qualification that enforcement is limited by laws relating to insolvency and creditors' rights is quite clearly proper. But it seems to me that an obligation is still valid and binding and enforceable notwithstanding that an action to enforce the obligation may subsequently become statute barred or that a right of set-off or counter-claim may be asserted. To me this qualification is therefore unnecessary.

I also consider unnecessary a qualification that any provision in the credit agreement which says that calculations shall be conclusive and binding will not apply where the same are fraudulent or manifestly inaccurate. I do not understand how a lender can expect to be able to enforce a calculation which has been fraudulently made or which is manifestly inaccurate, or if he wishes to attempt to enforce such a calculation that he could seriously expect to have recourse against the borrower's lawyer if he fails.

The next unnecessary qualification in my view is that no opinion is expressed on any provision that suggests that oral amendments and waivers will not be effective. I have a great deal of difficulty seeing how that could ever become an issue because the amendment if agreed to by the lender and agreed to within authority is going to be effective. If it is not going to be effective then I don't see how the lender is likely to turn around and complain.

The next qualification which I don't see any need for is that public records searched for the purposes of the opinion may not be complete or up to date. Suzanne has already mentioned the desirability of stating that you have searched the CAC records. It is certainly not unusual to specify this in an opinion, specifying that your opinion is based on searches carried out at or about a particular time at specified government offices. But there is no need for one to apologise for bureaucratic inefficiency. The statement as to the fact of the search is in

my opinion sufficient. After all if the lender does not know precisely what is available to be searched how can he complain as to the currency of the information searched. If he does know what is available to be searched he ought also to be aware of the delays in updating that information.

I can see that the position may be different where quite inordinate and unexpected delays have been experienced. For example, about twelve months ago the Papua New Guinea Companies Office moved from Port Moresby to Waigani, which is a distance of about seven miles. The office was closed for three months to effect the move. If you wanted to search in the meantime, your best bet was to ask a friend in the Justice Department to go down and find your client's cardboard box.

If the Victorian Corporate Affairs office was closed for three months it may well be desirable to disclose this fact in a Victorian law opinion, so as to dispel any suggestion that the opinion was based on current information.

The last area I want to deal with is the basis for the opinion. There are two real areas that the opinion is going to strike at. There are going to be the legal matters and there are going to be the factual bases for the opinion. The legal basis for the opinion is something well within your own control. You ought to be able to deal with it subject to one caveat, and that is that we are now used to waking up to the news that the Treasurer has announced some sweeping tax change or change in foreign investment guidelines. We rush to obtain a press release which is more often than not breathtaking in its simplicity (or, more accurately, in what it does not say, rather than what it says). From that point forward, of course, the law will be administered as if the announced change were legislatively effected. The lawyer ignores this at his peril since the legislation when finally introduced, if not previously superseded by something further qualifying the original release (a la withholding tax exemptions or dingoes), will be retrospective to the date of the original announcement.

The precise impact of the legislative changes foreshadowed by a press release will more often than not be difficult to predict unless or until the legislation becomes available. For example, when Division 16E of the Tax Act was first announced a number of concerns were raised and basically left unanswered. What if securities were issued at less than 100 percent - does the pricing matter? Would the new tax apply? Would there be similar exemptions as in the case of withholding tax? And so on.

Unsatisfactory as it may seem to all parties concerned, it is probably impractical for the borrower's lawyer to do any more than to refer to the press release and perhaps to engage in a little educated guesswork as to how the legislation may turn out. If he does engage in such guesswork he must make clear in his opinion that the exercise is one of conjecture rather than legal

analysis. Otherwise, if he is wrong he will be in peril. I think the best thing is probably to relax in the certain knowledge that whatever happens you will look a fool! The legislation never bears out the press release.

The area of fact is also an area of difficulty - more so nowadays where large corporations do not restrict themselves to one firm of lawyers. They deal with "horses for courses", they have large internal legal departments, the borrower's lawyer rarely knows much more about the corporation than the lender's lawyer. As a consequence the officer's certificate is becoming increasingly important to borrower's lawyers. Matters such as absence of proceedings for winding up, changes in memorandum and articles, non-revocation of powers of attorney, no regulations from general meetings superseding the powers of directors, no unregistered charges - they are all proper matters for reinforcement by officer's certificate as are certificates as to non-contravention of corporate agreements affecting a borrower. Nowadays it is impossible to know what BHP or Elders (or whatever) has signed itself up for, and the best you can hope for is a back to back certificate from your client - if you are unable to negotiate the relevant provision out of the opinion itself.