South Carolina Bar
Continuing Legal Education Division

2018 SC BAR CONVENTION

Corporate, Banking & Securities Law Section

Friday, January 19

SC Supreme Court Commission on CLE Course No. 180798

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FLSA for the General Corporate Counsel

Richard J. Morgan

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FLSA for the General Corporate Counsel

Presenter: Richard J. Morgan

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Fair Labor Standards Act

- Federal Minimum Wage: $7.25/hour
- Overtime: 1 ½ times the regular rate of pay for all hours over 40 hours in a work week

FLSA for the General Corporate Counsel

“White Collar” Exemptions

- Section 13(a)(1) of the FLSA provides an exemption from both minimum wage and overtime pay for employees who are employed in a bona fide:
- Executive;
- Administrative;
- Professional; or
- Outside Sales capacity.
- Certain computer employees may be exempt professionals under Section 13(a)(1) or exempt under Section 13(a)(17) of the FLSA.

Three Tests for Exemption

- Salary Level
- Salary Basis
- Job Duties

FLSA for the General Corporate Counsel

Salary Level

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Minimum Salary Level

- For most employees, the minimum salary level required for exemption is $455 per week/$26,660.00 per year
- Must be paid “free and clear”
- The $455 per week may be paid in equivalent amounts for periods longer than one week:
  - Biweekly: $1,025.38
  - Semimonthly: $1,110.83
  - Monthly: $2,221.67

Highly Compensated Test

- Total annual compensation of at least $100,000
- At least $455.00 per week paid on a salary or fee basis
- Perform office or non-manual work
- Customarily and regularly perform any one or more of the exempt duties identified in the standard tests for the executive, administrative or professional exemptions

Salary Basis

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Salary Basis Test

- Regularly receives a predetermined amount of compensation each pay period (on a weekly or less frequent basis)
- The compensation cannot be reduced because of variations in the quality or quantity of the work performed
- Must be paid the full salary for any week in which the employee performs ***any*** work
- Need not be paid for any workweek when no work is performed

Deductions from Salary

- An employee is not paid on a salary basis if deductions from the predetermined salary are made for absences occasioned by the employer or by the operating requirements of the businesses
- If the employee is ready, willing and able to work, deductions may not be made for time when work is not available

Permitted Salary Deductions

- Seven exceptions from the “no pay-docking” rule:

1. Absence from work for one or more full days for personal reasons, other than sickness or disability
2. Absence from work for one or more full days due to sickness or disability if deductions made under a bona fide plan, policy or practice of providing wage replacement benefits for these types of absences
3. To offset any amounts received as payment for jury fees, witness fees, or military pay

Permitted Salary Deductions (Cont.)

- Seven exceptions from the “no pay-docking” rule:

4. Penalties imposed in good faith for violating safety rules of “major significance”
5. Unpaid disciplinary suspension of one or more full days imposed in good faith for violations of workplace conduct rules
6. Proportionate part of an employee’s full salary may be paid for time actually worked in the first and last weeks of employment
7. Unpaid leave taken pursuant to the Family and Medical Leave Act

No Salary Requirements

- The salary level and salary basis tests do not apply to:
  - Outside Sales Employees
  - Doctors
  - Lawyers
  - Teachers (employed in an educational establishment and have a primary duty of teaching)
  - Certain computer-related occupations paid at least $27.63 per hour (If salary must be $455/week)

Review

- Minimum Salary Level: $455 per week
- Highly Compensated Level: $100,000 per year
- Salary Basis:
  - A predetermined amount paid for every week in which the employee performs any work, which is not subject to reduction because of variations in the quality or quantity of work performed
- The salary level and salary basis tests do not apply to outside sales employees, doctors, lawyers, teachers, and certain computer-related occupations paid at least $27.63 per hour

Executive Duties

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Executive Duties

- Primary duty is management of the enterprise or of a customarily recognized department or subdivision;
- Customarily and regularly directs the work of two or more other employees; and
- Authority to hire or fire other employees or whose suggestions and recommendations as to hiring, firing, advancement, promotion or other change of status of other employees are given particular weight.

Primary Duties

- The principal, main, major or most important duty that the employee performs.
- Factors to consider include, but are not limited to:
  - Relative importance of the exempt duties;
  - Amount of time spent performing exempt work;
  - Relative freedom from direct supervision; and
  - Relationship between the employee's salary and the wages paid to other employees for the same kind of nonexempt work.

Primary Duties

- Employees who spend more than 50% of their time performing exempt work will generally satisfy the primary duty requirement

- However, the regulations do not ***require*** that exempt employees spend more than 50% of time performing exempt work

Management

- Interviewing, selecting, and training employees
- Setting and adjusting pay and work hours
- Maintaining production or sales records
- Appraising employee productivity and efficiency
- Handling employee complaints and grievances
- Disciplining employees
- Planning and apportioning work among employees

Management

- Determining the techniques to be used; the type of materials, supplies, machinery, equipment or tools to be used; or the merchandise to be bought, stocked and sold
- Providing for the safety and security of employees or property
- Planning and controlling the budget
- Monitoring or implementing legal compliance measures

Department or Subdivision

- A “customarily recognized department or subdivision” must have a permanent status and continuing function
- Need not be physically within the employer’s establishment, and may move from place to place
- Continuity of the same subordinate personnel is not essential to the existence of a recognized unit.
- The employee in charge of each branch establishment is in charge of a recognized subdivision
- Does not include a mere collection of employees assigned from time to time to a specific job

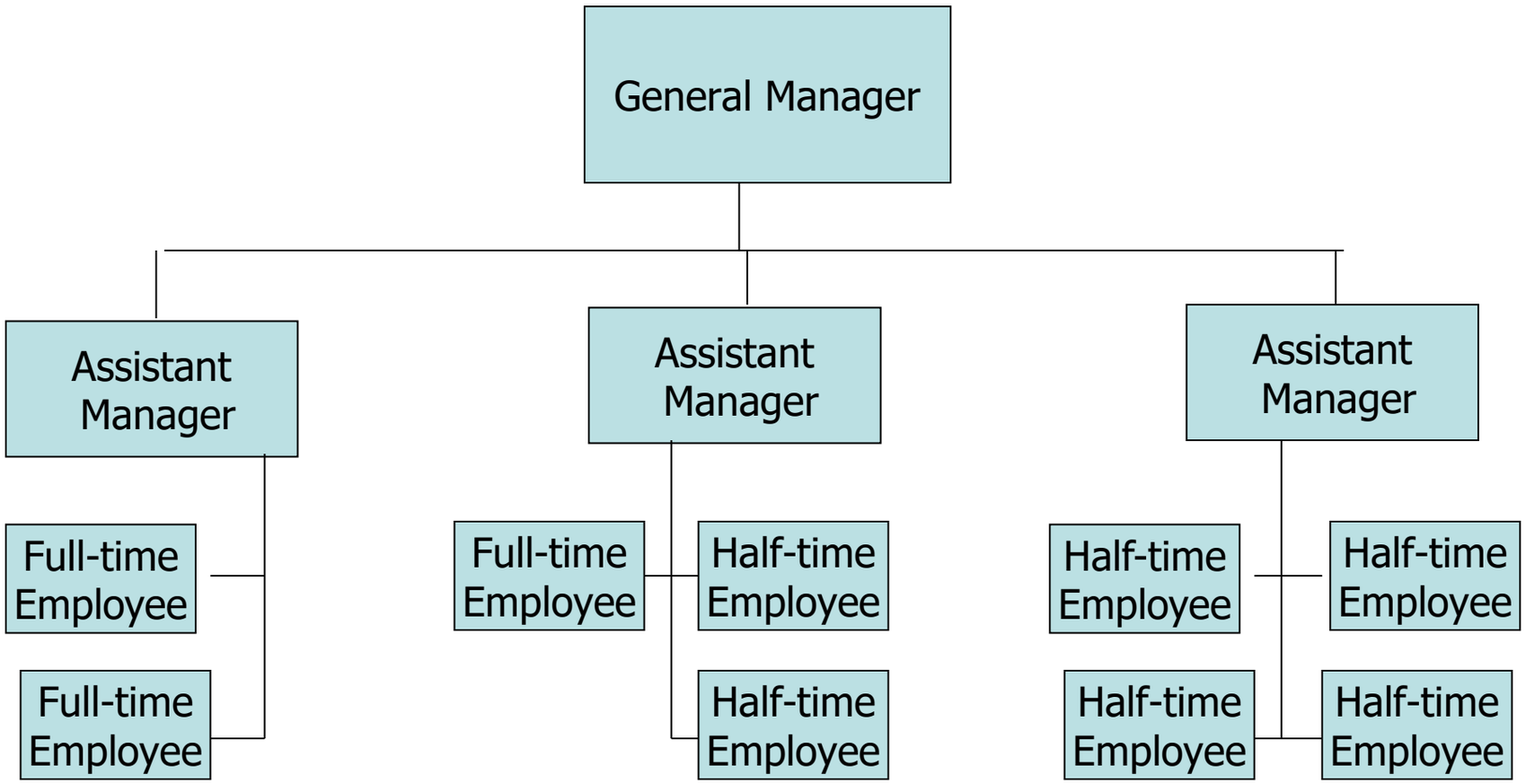
Customarily and Regularly

- A frequency that must be greater than occasional but which, of course, may be less than constant
- Includes work normally and recurrently performed every workweek
- Does not include isolated or one-time tasks

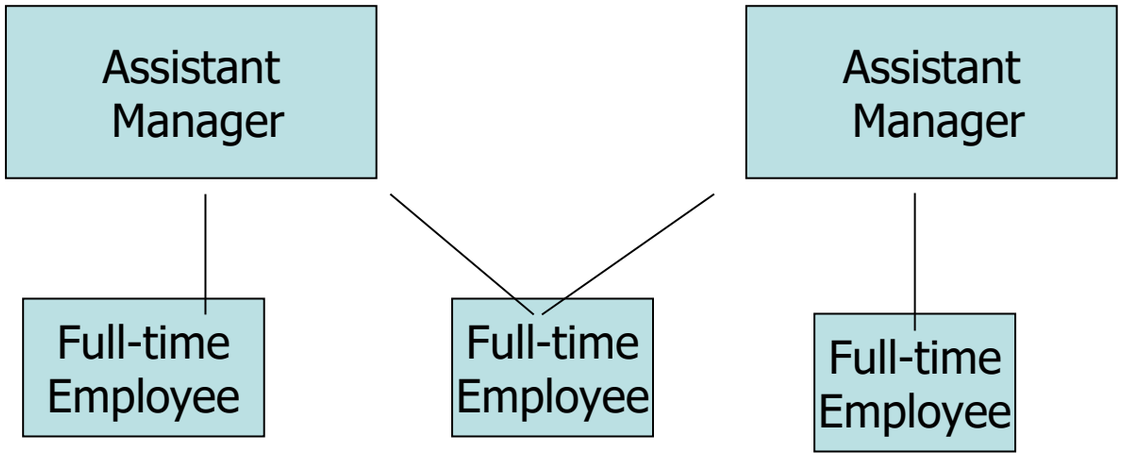
Two or More

- The phrase “two or more other employees” means two full-time employees or the equivalent
- Full-time generally means 40 hours per week
- The supervision of the same employees can be distributed among two or more exempt executives, but the hours worked by an employee cannot be credited more than once

Staffing Meeting the Two or More



Staffing That Does NOT Meet the Two or More



20% Owner Executives

- The executive exemption also includes employees who:
  - own at least a bona fide 20-percent equity interest in the enterprise; and
  - are actively engaged in management of the enterprise.
- The salary level and salary basis requirements do not apply to 20% equity owners.

Review

- Duties requirements for executive exemption:
  - Primary duty of management;
  - Customarily and regularly directs the work of two or more other employees; and
  - Authority to hire or fire or having suggestions and recommendations as to hiring, firing, advancement promotion or any other change of status to other employees be given particular weight.
- The executive exemption also applies to 20% owners who are actively engaged in management.

Administrative Duties

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Administrative Duties

- Whose primary duty is the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- Whose primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

Management or General Business Operations

- Refers to the type of work performed by the employee
- Work must be directly related to assisting with the running or servicing of the business
- Does not include working on a manufacturing production line or selling a product in a retail or service establishment

Management or General Business Operations

- Tax
- Finance
- Accounting
- Budgeting
- Auditing
- Insurance
- Quality Control
- Purchasing
- Procurement
- Advertising
- Marketing
- Research
- Safety and Health
- Human Resources
- Employee Benefits
- Labor Relations
- Public and Government Relations
- Legal and Regulatory Compliance
- Computer Network, Internet and Database Administration

Discretion and Independent Judgement

- The comparison and evaluation of possible courses of conduct, and acting or making a decision after the various possibilities have been considered
- Must be exercised with respect to “matters of significance,” which refers to the level of importance or consequence of the work performed
- Decisions and recommendations may be reviewed at a higher level and, upon occasion, revised or reversed

Discretion and Independent Judgement

- Factors include, but are not limited to:
  - Whether the employee has authority to formulate, affect, interpret, or implement management policies or operating practices
  - Whether the employee carries out major assignments in conducting the operations of the business
  - Whether the employee performs work that affects business operations to a substantial degree, even if the employee's assignments are related to operation of a particular segment of the business

Discretion and Independent Judgement

- Factors include, but are not limited to:
  - Whether the employee has authority to commit the employer in matters that have significant financial impact
  - Whether the employee has authority to waive or deviate from established policies and procedures without prior approval
  - Whether the employee has authority to negotiate and bind the company on significant matters
  - Whether the employee provides consultation or expert advice to management

Discretion and Independent Judgement

- Factors include, but are not limited to:
  - Whether the employee is involved in planning long- or short-term business objectives
  - Whether the employee investigates and resolves matters of significance on behalf of management
  - Whether the employee represents the company in handling complaints, arbitrating disputes or resolving grievances

Insurance Claims Adjusters

- Exempt status depends on actual job duties
- May be exempt if duties include:
  - Interviewing insureds, witnesses and physicians
  - Inspecting property damage
  - Reviewing factual information to prepare damage estimates
  - Evaluating and making recommendations regarding coverage of claims
  - Determining liability and total value of a claim;
  - Negotiating settlements
  - Making recommendations regarding litigation

Financial Services

- May be exempt if duties include:
  - Collecting and analyzing information regarding the customer's income, assets, investments or debts
  - Determining which financial products best meet the customer's needs and financial circumstances
  - Advising the customer regarding the advantages and disadvantages of different financial products
  - Marketing, servicing or promoting the employer's financial products
- An employee whose primary duty is selling financial products does not qualify for the administrative exemption

Human Resources

- Human resource managers who formulate, interpret or implement employment policies generally meet the administrative duties requirements
- Personnel clerks who “screen” applicants to obtain data regarding minimum qualifications and fitness for employment generally are not exempt administrative employees

Other Exempt Positions

- An employee who leads a team of other employees assigned to complete major projects

- Executive assistant or administrative assistant to a business owner or senior executive of a large business who has been delegated authority regarding matters of significance

- Management consultants who study the operations of a business and propose changes in organization

Review

- Primary duty of the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- Primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

Learned Professionals Duties

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Learned Professional

- The employee's primary duty must be the performance of work requiring advanced knowledge
- In a field of science or learning
- Customarily acquired by a prolonged course of specialized intellectual instruction

Creative Professional Duties

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Creative Professional Duties

- The employee's primary duty must be the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor

Recognized Field of Artistic or Creative Endeavor

- Music
  - Musicians, composers, conductors, soloists
- Writing
  - Essayists, novelists, short-story writers, play writers
  - Screen play writers who choose their own subjects
  - Responsible writing positions in advertising agencies
- Acting
- Graphic Arts
  - Painters, photographers, cartoonists

Invention, Imagination, Originality or Talent

- A creative professional must perform work requiring invention, imagination, originality or talent
- Creative professional work ***does not*** include:
  - Work that primarily depends on intelligence, diligence and accuracy
  - Work that can be produced by a person with general manual ability and training
- Exempt status is determined on a case-by-case basis, depending on the extent of the invention, imagination, originality or talent exercised

Review

- Learned Professional
  - Primary duty of the performance of work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction
- Creative Professional
  - Primary duty of the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor

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Rick is certified by the South Carolina Supreme Court as a specialist in employment and labor law. He represents employers and has tried to verdict numerous employment defamation, discrimination, harassment and retaliation cases.

Rick advises and counsels employers on all aspects of employment and labor law issues and has experience representing employers in state and federal courts and in administrative tribunals. He has defended employers in litigation involving wage and hour laws, unemployment compensation, unfair labor practices, contract disputes, wrongful termination, negligent supervision/hiring/retention, intentional infliction of emotional distress, conspiracy and enforcement of non-compete agreements. In addition, Rick has advised employers during union organizing attempts and in OSHA matters. Rick is a part-time City of Columbia Municipal Court Judge.

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I. INTRODUCTION

The Fair Labor Standards Act ("FLSA") is the federal law passed in 1938 to regulate minimum wages, overtime pay, equal pay and child labor standards in employment. Today's employers are now faced with issues ranging from telecommuting by employees to flexible scheduling arrangements, yet still are responsible for understanding and complying with the same statute which was initially enacted to address a primarily industrial workplace. This paper will not address detailed FLSA enforcement nor FLSA litigation.

A. WHO IS COVERED UNDER THE FLSA?

1. COVERED EMPLOYERS

The FLSA has very broad coverage. An employer does not need to employ a threshold number of employees to be covered. You must comply with the FLSA if your organization

- Is engaged in interstate commerce and has annual gross income of $500,000; or
- Is a public agency; or operates a hospital, health care facility or school.

States are immune from suit under the 11th Amendment unless such immunity is waived; however, subdivisions of a state, such as municipalities and state-funded agencies, are not immune from suit under the FLSA. Although the Court ruled that states may not be sued by employees for alleged FLSA violations, they may still be sued on behalf of employees by the Secretary of Labor.

An employer under the FLSA is defined to include any person acting directly or indirectly in the interest of an employer in relation to an employee and *may include individuals* such as owners, officers, directors, managers or supervisors, if they have a sufficient amount of control over the applicable pay policies or practices.

See, 29 U.S.C. §§ 202(d); 203(j).

2. COVERED EMPLOYEES

The FLSA also covers individual employees who are engaged in interstate commerce, produce goods for commerce, or work in activities closely related to such work. This includes activities such as traveling to other states, using mail, e-mail, or telephones for interstate communications, shipping or receiving goods to or from other states. Therefore, even if an employer is not covered by the FLSA, most of if not all of its employees will typically be individually covered. Very few employers of any size are free of obligations under the FLSA.

a. <u>Contract Workers</u>

Some employers seek to avoid the obligations and potential liability presented by the FLSA and other employment laws by classifying workers as "independent contractors," and paying them by means of the 1099 process, rather than through payroll. Some such classifications are appropriate. However, the fact that an employer labels a worker as a contractor is not controlling. The question will be the economic reality of the relationship - "economically dependent on the business to which he renders service,...or is, as a matter of economic fact, in business for himself."

In deciding whether an individual is an "employee" generally consider the following factors:

- The degree of the alleged employer's right to control the manner in which the work is to be performed (the more control you have over an individual, the more likely she will be deemed an employee)
- The alleged employee's opportunity for profit or loss depending upon his or her managerial skill
- Whether the alleged employee provides the equipment or materials required for his or her task or whether he or she employs helpers
- The degree of permanence of the working relationship
- Whether the service rendered requires a special skill
- Whether the service is an integral part of the employer's business

No one factor alone is determinative. The DOL will weigh all factors when considering whether an individual has been correctly classified as a contractor. If the DOL finds you have incorrectly classified a worker, you will be obligated to pay any overtime worked while the worker was performing services for your company.

See, 29 U.S.C. §§ 203(e) (1), 206, 207(a) (1).

b. <u>Unpaid Workers</u>

i. Trainees

Trainees are not employees under the FLSA if the following criteria are met: (a) The training is similar to that which would be given at a vocational school; (b) The training is for the benefit of the trainees; (c) The trainees do not displace regular employees and work under close observation; (d) The employer that provides training derives no immediate advantage from the activities of the trainees, and its operations may actually be impeded; (e) The trainees are not necessarily entitled to a job at the completion of the training; (f) The employer and the trainees understand that the trainees are not entitled to wages for the time spent in training.

ii. Volunteers

If the following requirements are met, the worker will be considered a volunteer and not an employee under the FLSA: (a) The services must be offered freely and without pressure or coercion; (b) The volunteer must not receive or expect any compensation other than being paid expenses, reasonable benefits, or a nominal fee for performing the services; (c) The services must be different from any service that the individual is employed to perform for the employer.

Volunteers are specifically exempted from all of the statutory requirements of the FLSA.

3. JOINT EMPLOYMENT

Employers should also bear in mind that they may be a "joint employer" of an employee covered by the FLSA. If an employee has been hired by two or more employers or works for two or more employers and the employers are considered joint employers, time worked for all employers must be totaled for purposes of calculating overtime.

Under the FLSA a joint relationship exists when: (a) An arrangement exists between the employers to share the employee's services; or (b) One employer is acting directly or indirectly in the interest of the

other employer in relation to the employee; or (c) The employers share control of the employee because one employer controls or is under common control with the other employer.

See, 29 C.F.R. §§ 776.3; 791.1.

4. SUBJECT MATTER COVERED BY FLSA

The requirements of the FLSA extend to the following issues: (a) Minimum wage (making sure non-exempt employees have been compensated at least minimum wage for all hours actually worked); (b) Overtime (making sure non-exempt employees have been compensated at the applicable overtime rate for all hours worked over 40 in a workweek); (c) Recordkeeping (making sure employers keep accurate records of work time and compensation for all non-exempt employees); (d) Exemptions (verifying that employees who are treated as exempt from the FLSA's provisions have been accurately classified); (e) Equal pay (making sure women receive pay equal to men, for equal work); (f) Enforcement of child labor laws; (g) Timely payment of wages and overtime.

The FLSA does not apply to issues pertaining to: (a) Paid leave (establishment or implementation of policies pertaining to accrual of, deduction from, and/or payment of vacation, holiday, or sick pay, PTO, personal leave, etc.); (b) Mandatory meal or rest periods; (c) Daily overtime (for example, working over 8 hours per day); (d) Shift premiums or premium pay for working weekend or holiday work; (e) Reimbursement for mileage; (f) Pay raises; (g) Benefits; (h) Termination (except that termination in retaliation for complaining about pay issues is prohibited); (i) Payment of final wages to terminated employees or (j) Limitations on the number of hours in a day or days in a week an employee may be required to work, including overtime hours (if the employee is at least 16 years old); (k) Contractual disputes between employers and employees pertaining to compensation and other issues (individual contracts and collective bargaining agreements).

Some of these issues are governed by other federal laws, such as ERISA, which governs certain employee benefits programs, or the NLRA, which governs wages under collective bargaining agreements, and beyond the scope of this presentation.

II. OVERVIEW OF FLSA REQUIREMENTS

A. RECORD KEEPING

The FLSA requires employers to make, keep, and preserve records containing the following information regarding employees and employee compensation: (a) Name and social security number; (b) Home address, including zip code; (c) Date of birth, if under age 19; (d) Sex and occupation; (e) Time of day and day of the week on which employee's workweek begins; (f) The hourly rate of pay; (g) The basis of pay; (h) The nature of each payment which is claimed as an exclusion from the regular rate; (i) Total hours worked for each day and each week; (j) Total straight (i.e., non-overtime or premium) pay; (k) Total overtime pay; (l) Additions and deductions made, including wage assignments; (m) Total wages paid; (n) Date of payment and pay period covered; (o) The company's sales and purchase records for purposes of determining whether it is an enterprise with an annual business volume of $500,000.

Under the Act, all records which constitute the primary sources of this information must be preserved for a period of three years, for all current and former employees. Such records include payroll records, work certificates, collective bargaining agreements, and individual employment contracts.

Supplementary records—documents serving as the source documents for other payroll records maintained by an employer—must be preserved for at least two years. Supplementary records may include time cards, production cards, wage rate tables, piece-rate schedules, and work-time schedules.

The FLSA requires that all records be kept at the place or places of employment or at one or more established central record-keeping offices where such records are customarily maintained. If kept at a central record-keeping office rather than the place of employment, the records must be available within 72 hours following a request by the DOL.

Federal regulations also require covered employers to post notices in the workplace stating the requirements of the FLSA.

See, 29 C.F.R. § 516.2-7.

B. CHILD LABOR

The child labor provisions in the FLSA restrict the amount of time and conditions under which minors age 17 and younger are permitted to work (with exceptions for minors engaged in farm work). Youths age 16 to 17 may perform any non-hazardous job for unlimited hours. Those ages 14 and 15 may work outside school hours in various jobs (except manufacturing, mining and hazardous positions) under the following conditions: (a) They can't work more than three hours on a school day, 18 hours in a school week, eight hours on a non-school day in a non-school week or 40 hours in a non-school week; (b) Between Labor Day and May 31, they can't begin work before 7 a.m. or end after 7 p.m. From June 1 through Labor Day, their work must end before 9 p.m.

Children under 14 are not allowed to work, except in a few limited circumstances, including delivering newspapers, performing in radio, television, movie, or theatrical productions and working in their parent's solely owned business.

See, 29 U.S.C. § 212; 29 C.F.R. § 570

C. EQUAL PAY

The Equal Pay Act (which amended the minimum wage provisions of the FLSA and is subject to enforcement under the FLSA) requires that men and women be given equal pay for equal work in the same establishment. The jobs need not be identical, but they must be substantially equal. It is job content, not job titles, that determines whether jobs are substantially equal.

Employers may not pay unequal wages to men and women who perform jobs that require substantially equal skill, effort and responsibility, and that are performed under similar working conditions within the same establishment. Factors are summarized below:

- **Skill** - Measured by factors such as the experience, ability, education, and training required to perform the job. The key issue is what skills are required for the job, not what skills the individual employees may have. For example, two bookkeeping jobs could be considered equal under the EPA even if one of the job holders has a master's degree in physics, since that degree would not be required for the job.

- **Effort** - The amount of physical or mental exertion needed to perform the job. For example, suppose that men and women work side by side on a line assembling machine parts. The person at the end of the line must also lift the assembled product as he or she completes the work and places it on a

board. That job requires more effort than the other assembly line jobs if the extra effort of lifting the assembled product off the line is substantial and is a regular part of the job. As a result, it would not be a violation to pay that person more, regardless of whether the job is held by a man or a woman.

- **Responsibility** - The degree of accountability required in performing the job. For example, a salesperson who is delegated the duty of determining whether to accept customers' personal checks has more responsibility than other salespeople. On the other hand, a minor difference in responsibility, such as turning out the lights at the end of the day, would not justify a pay differential.

- **Working Conditions** - This encompasses two factors: (1) physical surroundings like temperature, fumes, and ventilation; and (2) hazards.

- **Establishment** - The prohibition against compensation discrimination under the EPA applies only to jobs within an establishment. An establishment is a distinct physical place of business rather than an entire business or enterprise consisting of several places of business. However, in some circumstances, physically separate places of business should be treated as one establishment. For example, if a central administrative unit hires employees, sets their compensation, and assigns them to work locations, the separate work sites can be considered part of one establishment.

Pay differentials are permitted when they are based on seniority, merit, quantity or quality of production, or a factor other than sex. In correcting a pay differential, no employee's pay may be reduced. Instead, the pay of the lower paid employee(s) must be increased.

See, 29 U.S.C. § 206(d)(1).

D. MINIMUM WAGE

The current minimum wage under the FLSA is: July 24, 2009 – $7.25

Some states set higher minimum wages than the federal government, and you must always comply with the stricter law in each jurisdiction in which you have employees. Also, bear in mind that some municipalities have enacted "living wage" laws mandating even higher pay rates.

See, 29 U.S.C. § 206;

1. EXEMPTIONS FROM MINIMUM WAGE

Although the minimum wage component of FLSA compliance is generally pretty easy to apply, there are a few wrinkles which you may have to iron out: **a. Teenagers - *Applicable law:*** 29 U.S.C. § 214; **b. Apprentices and learners - *Applicable law:*** 29 U.S.C. § 214; **c. Workers with disabilities under special certificates - *Applicable law:*** 29 U.S.C. § 214.

2. TIPPED EMPLOYEES

There is a limited exception to the minimum wage requirements for tipped employees. Workers who regularly receive more than $30 a month in tips are considered "tipped employees." Employers may claim a tip credit against their minimum-wage obligations to such employees, so long as they pay the tipped employees a cash wage of at least $2.13 an hour. Employers should require tipped employees to carefully record and report all tips received each pay period. If an employee's tips and cash wages together don't equal at least the minimum wage for all hours worked, the employer must make up the difference.

The tip credit doesn't apply unless the employee has been made aware of the credit provisions and has been allowed to retain all the tips she received.

See 29 U.S.C. § 203 (m) and (t).

3. PIECE RATES

An employee working on a piece-rate basis (paid based on rate of production rather than time worked) must earn at least the minimum wage. Examples of piece rate work include: (a) Servers employed by a catering service who are paid a flat rate per event; (b) Transcriptionists employed by a hospital, who are paid according to the number of lines transcribed; (c) Garment workers paid according to the number of garments completed.

To determine whether a piece rate worker is receiving at least minimum wage, divide the employee's total earnings for the workweek by the number of hours worked that week.

4. COMMISSIONS

Employees paid either partially or solely on a commission basis must receive at least the minimum wage for weeks in which their earnings fall short of the minimum wage. Also, you can't recover any part of the minimum-wage payment from the employee's earnings in weeks when his commissions exceed the minimum wage.

5. PAYROLL DEDUCTIONS

The general rule is that you cannot make payroll deductions that cut the employee's pay to a level below the minimum wage. Examples of such illegal deductions include: (a) Fines for infractions, poor work, or other disciplinary reasons; (b) Deductions for damage to company property; (c) Repayment of shortages; (d) Repayment for employee theft, unless the employee has been convicted; (e) Voluntary payments from an employee that don't involve payroll deductions, such as deposit or cash bond required from an employee at the time of hiring; (f) Wardrobe costs deducted from paychecks to cover employee clothing purchases when dressing in the store's signature style is encouraged

Remember, these kinds of deductions are not illegal in and of themselves under the FLSA—they are only illegal if they result in an employee being paid less than minimum wage for the applicable pay period. Also keep in mind that many states have their own laws addressing these issues, which may impose stricter standards.

The DOL has determined that employers are permitted to make certain deductions, even if they do bring the employee's pay below the minimum wage: (a) Taxes; (b) Reasonable cost of board and lodging; (c) Union dues; (d) Insurance premiums paid; (e) Payments to independent insurance companies; (f) Savings plans requested by the employee; (g) Repayment of loans, as long as the employer has no connection to the lender; (h) Repayment of free-and-clear cash advances by an employer to an employee (but not a loan, with interest, from an employer to an employee); (i) Payments on store accounts at the employee's request if the stores are wholly independent of the employer; (j) Wage attachments, garnishments (but beware of possible state limitations); (k) Deductions for absences (but only equivalent to the amount of time missed).

E. OVERTIME

The FLSA provides that, in addition to minimum wage, employees must be paid overtime at a rate of not less than one and a half times their regular hourly rate for all hours worked over 40 during a 7-day workweek.

1. FLSA WORKWEEK

For purposes of calculating overtime, an employee's workweek is a fixed and regularly recurring period of 168 hours—seven consecutive 24-hour periods. The workweek need not coincide with the calendar week but may begin on any day and hour. An employer may choose any 7-day workweek, but it needs to be consistent and not change the workweek once chosen. Different workweeks may be established for different employees or groups of employees.

See, 29 U.S.C. § 207(j) (14-day work period for hospital employees).

2. TIMING OF OVERTIME PAY

The FLSA does not require that overtime be paid weekly. The general rule is that overtime pay earned in a particular workweek must be paid on the regular payday for the period in which the workweek ends. If the correct amount of time cannot be determined until sometime after the regular pay period, the employer must pay the overtime compensation as soon as is practicable.

See, 29 C.F.R. § 778.105; 29 C.F.R. § 778. 106.

3. COMPENSATORY TIME IN LIEU OF OVERTIME

Some employers utilize systems where they require, or permit, employees to "bank" overtime hours to use as paid leave in the future. In most instances, this practice is illegal under the FLSA.

a. Private Employers

Private employers are not permitted to offer employees compensatory time off (or "comp time") instead of paying overtime. An employer may rearrange an employee's hours within a pay period (even over two workweeks) to avoid overtime.

b. Public Employers

Public sector employers may provide compensatory time off ("comp time") in lieu of overtime pay as long as the employees agree to do so and the agreement is embodied in a collective bargaining agreement or some other understanding reached between the employer and employee prior to the performance of the work in question. Comp time systems must comply with the requirements set forth in the FLSA and federal regulations, or they will be deemed invalid, subjecting the employer to liability for overtime back pay for all banked hours.

Comp time must accrue at the rate of one and one half hours of comp time for every hour of overtime worked. In general, public sector employees may accrue up to 240 hours of comp time (480 hours for employees engaged in public safety emergency response or a seasonal activity). Employers must honor requests to use comp time within a reasonable period of time following the request, as long as the time off does not unduly disrupt operations.

If employees do not use their accumulated compensatory time, the employer is obligated to pay cash compensation under certain circumstances, including upon termination.

See, 29 U.S.C. § 207(o).

III. PAYING EMPLOYEES CORRECTLY

For all non-exempt employees, you must determine whether they are entitled to overtime in a particular pay period, and how much you owe them. To do this, you have to first know how to count the number of hours an employee works in a given workweek. Second, you must be able to correctly calculate his regular rate of pay, which is not necessarily the same thing as his hourly rate. Calculation of the regular and overtime rates requires an understanding of what amounts are, and are not, included in an employee's compensation for the workweek.

A. HOURS WORKED

The first step in determining how much an employee is owed is determining how many hours he has worked during each seven-day workweek covered by the employer's pay period. Federal regulations state that ***"work not requested but suffered or permitted is work time."*** The first thing you must understand in applying this rule is that you must pay employees for all time worked, whether the work was requested, authorized, or even needed.

See, 29 C.F.R. §§ 785.11-12.

1. TRACKING TIME

The FLSA requires employers to keep accurate time records for all non-exempt employees. This is true regardless of how employees are paid—accurate time records must be kept for workers paid by salary, day rate, piece rate, commission, or any other method of compensation, unless they qualify for one of the overtime exemptions.

Federal regulations do not require any particular method of record keeping; however, a method which tracks the **actual time worked is required**.

See, 29 C.F.R. § 785.23.

2. ROUNDING/*DE MINIMIS* DOCTRINE

The general rule is that all time worked is compensable. However, the *de minimis* doctrine permits employers to treat very small increments of time as non-compensable. This means that, if an employee occasionally works for a few minutes "off the clock," either at home or before clocking in at work, the employer does not need to trouble itself with tracking this time. To be *de minimis*, activities must be so "insubstantial and insignificant" that they ought not to be included as part of the workweek "[A] few seconds or minutes of work beyond the scheduled working hours… may be disregarded." Factors in determining whether time is *de minimis* are: (a) The practical administrative difficulty of recording the additional time; (b) The size of the claim in the aggregate; and (c) Whether the work is performed on a regular basis.

The *de minimis* rule also permits "rounding" an employee's time to the nearest ten minute increment. However, as a general rule, if an employee works ten minutes or longer, an employer must make sure the time is captured and compensated.

See, Anderson v. Mt. Clemens Pottery Co., 328 U.S. 680, 66 S.Ct. 1187, 90 L.Ed. 1515 (1946); *Lindow v. United States*, 778 F.2d 1057, 1062-63 (9th Cir. 1984) (holding that an average of seven to eight minutes of pre-shift activity is *de minimis*); *Reich v. Montfort, Inc*., 144 F.3d 1329 (10th Cir. 1998) (citing *Anderson v. Mt. Clemens Pottery Co*., 328 U.S. 680 (1946)).

4. SPECIFIC WORK TIME ISSUES

Here is an overview of issues which frequently arise as employers attempt to determine what is, and what is not, compensable work time.

a. <u>On-call time</u>

Employees required to remain "on call" on the employer's premises (or so close that they can't use the time for their own purposes) must be considered to be working. Even when employees aren't required to remain at work, however, their "on call" time may be compensable. Two factors determine whether on-call time is compensable work time: (a) Whether the wait predominantly benefits the employer; and (b) Whether employees are able to use the time for their own purposes.

Factors frequently considered in determining whether on-call time is compensable include: (a) Required response time; (b) Use of a pager to ease restrictions; (c) Ability to trade on-call shifts; (d) Excessive geographical limitations; (e) The employee's ability to engage in personal activities; (f) Frequency of calls.

See, 29 C.F.R. § 785.17; 29 C.F.R. § 553.221(d).

b. <u>Meals and rest periods</u>

The DOL requires that employees be paid for all breaks of less than 30 minutes. This means that an employee cannot be docked for lunch breaks, smoke breaks, telephone breaks, and the like unless you require those breaks to be at least 30 minutes long.

The test: "completely relieved from duty for the purpose of eating regular meals." In determining whether meal periods or other longer rest breaks are compensable time, examine: (a) The restrictions placed upon the employee; (b) The extent to which these restrictions benefit the employer; (c) The duties of the employee during the break period; and (d) The frequency of interruption.

The FLSA does not require employers to give employees breaks or meal periods.

See, 29 C.F.R.§ 785.18-19.

c. <u>Sleep time</u>

Under the FLSA, for employees whose shifts are less than 24 hours long, any time in which an employee is permitted to sleep is compensable. However, if the employees are required to be on duty for more than 24 hours, up to eight hours of sleep time may be excluded from compensation by agreement between an employer and employee if the employee's sleep time is not interrupted for at least five hours of that period and the employer provides adequate sleeping facilities. In the case of employees who reside on site, the parties may also agree on additional amounts of private time to be excluded from hours worked.

See, 29 C.F.R. § 785.21-23.

d. Preliminary/Postliminary time

The Portal to Portal Act generally excludes an employee's preliminary and postliminary activities from the minimum wage and overtime provisions of the FLSA. This general exemption does not apply, however, if there is a contractual obligation or custom and practice which provides that employees are paid for this time. Pre- and post-work activities are compensable, however, if they are an "integral" and "indispensable" part of the employee's principal activities. Preliminary and postliminary work is not compensable if it falls under the *de minimis* exception.

See, 29 U.S.C. § 254.

e. Idle time/Waiting time

Preliminary and postliminary waiting time which is not for the benefit of the employer is not compensable work time. For instance, waiting time spent in a paycheck line, to check in or out at a time clock, or to start work at a designated period, is not work time. When looking at whether waiting time is compensable, ask whether the employee is waiting to be engaged (not compensable) or being engaged to wait (compensable).

See, 29 C.F.R. § 785.15-16.

f. Commuting time

Ordinary commuting time between home and work is generally not considered compensable time, even for employees whose work sites may vary.

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See, 29 U.S.C. § 254(a); 29 C.F.R. § 785.35; 29 C.F.R. § 785.41.

g. Travel time

Determining whether time spent in travel is working time can be challenging, and depends on the kind of travel involved.

See, 29 U.S.C. § 254(b); 29 C.F.R. § 785.35 & § 785.38.

i. One-Day Out-of-Town Assignments

When an employee who regularly works at a fixed location in one city is given a special one-day work assignment in another city, the time spent traveling from home to the airport is not considered work time and is not compensable. Additionally, meal periods are not compensable. But, all of the remaining time away from home would be considered working time, and is compensable, even if the time spent away from home exceeds the employee's normal work day.

See, 29 U.S.C. § 254(b); 29 C.F.R. § 785.38.

ii. Overnight travel

Overnight travel during the employee's regular working hours or their weekend equivalent is also compensable. For instance, an employee must be paid for traveling between 9 a.m. and 5 p.m. on Saturday if that employee works 9 a.m. to 5 p.m. during the week.

See, 29 U.S.C. § 254(b); 29 C.F.R. § 785.39.

h. Changing clothes

Time spent changing clothes is compensable if this activity "is indispensable to the performance of the employee's work or is required by law or by the rules of the employer." Donning required uniforms or protective gear would be an example of compensable work time, as recently confirmed by the United States Supreme Court. You should be aware, however, that the FLSA contains a provision which excludes from compensable time all time spent by employees in changing clothes when such time is excluded under "the express terms of or by custom or practice under a bona fide collective bargaining agreement...."

See, 29 C.F.R. § 785.26; 29 U.S.C. § 203(o).

i. Training

Employers must pay an employee for time spent attending training programs, seminars, and lectures, **unless ALL of the following factors apply**: (a) Attendance is outside regular working hours; (b) Employee doesn't perform any productive work during the sessions; (c) The program doesn't directly relate to the employee's job; (d) Attendance is voluntary.

If the training is intended to help the employee perform her job better, then it is directly related to her job and must be compensated. But if the purpose of the training is to enhance an employee's skills or qualifications for promotion or advancement, so long as you have not required the employee to attend, you do not have to pay for the training time.

See, 29 C.F.R. § 785.27-32.

j. Charitable/Civic activities

Employers must pay an employee for hours spent on civil or charitable work if: (a) The activity takes place during regular working hours; (b) If outside of normal work time, it is the same type of work the employee would do as part of her job; (c) You require employees to participate.

Employers are not required to pay for civic or charitable work if: (a) The activity does not take place during normal working hours; (b) You don't require participation or penalize those who don't; (c) The duties performed are different from the employee's normal work duties.

See, DOL Opinion Letter, January 27, 2006.

B. CALCULATING THE REGULAR AND OVERTIME RATE

Before computing the amount of overtime pay to which an employee is entitled in a particular week, you must first determine her regular hourly rate of pay. An employee's "regular rate" can never be less than the federal minimum wage or other applicable minimum wage, if higher. The correct way to determine an employee's regular rate depends on how the employee is being compensated. Once you have figured out the regular rate, generally, the overtime rate will be one-and-a-half times that number.

1. PAYMENT ON AN HOURLY BASIS

If an employee is paid solely on an hourly basis, this computation is simple—the regular rate is the same as the employee's hourly rate of pay, and the overtime rate is 1.5 times that amount.

2. PAYMENT AT DIFFERENT HOURLY RATES

An employee may be paid different hourly rates during the week, depending on the type of work he is performing. Or, you may employ an individual who works for you in two or more different positions during the same workweek, at different rates of pay—if that is the case, the general rule is you must count all hours worked in all positions and at all rates towards the weekly total for purposes of determining whether the employee is owed overtime. When an employee receives different hourly rates of pay throughout the week, generally, you determine the regular rate by dividing the total compensation received during the workweek by the total number of hours worked. This will produce a "weighted average" or "blended" rate.

Under certain circumstances, an employer and an employee may agree that the overtime rate for an employee working at two or more rates during a workweek will be calculated on an alternative basis.

3. PAYMENT ON A SALARIED BASIS

If a non-exempt employee is paid on a salaried basis, you still have to figure out the hourly rate in order to calculate the amount of overtime pay owed. You do this by dividing the amount of the employee's weekly salary by the number of hours the salary is intended to compensate. If the employee's salary basis is covering something other than a week, the salary must be reduced to its weekly equivalent. (For instance, a monthly salary must be multiplied by 12, then divided by 52, whereas a semi-monthly salary must be multiplied by 24, then divided by 52.)

If the employee works variable hours, his regular rate will differ from week to week. Remember, you have to make this calculation based on the number of hours actually worked by the employee, rather than his regularly scheduled hours.

See, 29 C.F.R. § 778.113.

4. FIXED SALARY FOR FLUCTUATING HOURS

Suppose a non-exempt employee's salary is not intended to compensate a given number of hours (such as the 37.5 in the example above) but is intended to cover whatever hours are worked during the week? For example, what if you wish to pay an employee $500 per week, regardless of whether 10 hours are worked, or 50 hours? If there is a clear mutual understanding between you and the employee on this issue, you may take advantage of a more favorable way of calculating overtime, under what is known as a the "fluctuating workweek method." For an employer to be able to use this method, federal regulations require: (1) There is a clear mutual understanding between the parties; (2) The employee's hours fluctuate from week to week; (3) The employee receives the same fixed salary regardless of the number of hours worked during a particular week; (4) The salary provides an average hourly rate of more than the minimum wage; and (5) The employee receives pay, in addition to salary, for overtime hours worked.

The regular rate under the fluctuating hours method is calculated by dividing the employee's salary by the actual hours worked in a given workweek. **The employer need only pay 1/2 this regular rate (as opposed to 1½ times the regular rate) multiplied by the hours worked over 40.** While this method poses some difficulties in administration, the reduced overtime rate generally results in greater cost savings to the employer.

See, 29 C.F.R. § 778.114(a).

5. PIECE RATE/DAY RATE PAYMENT

If the employee is paid a flat sum for a day's work or for doing a particular job, without regard to the number of hours worked in the day or on the job, and if he receives no other form of compensation for services, his regular rate is determined by totaling all of the sums received at such day rates or job rates in the workweek in question and dividing by the total hours actually worked. The employee is then entitled to extra half-time (not 1 ½ time) pay at this rate for all hours worked in excess of 40 in the workweek.

When an employee is employed on a piece-rate basis, his regular hourly rate of pay is computed by adding together his total earnings for the workweek from piece rates and all other sources, then dividing this sum by the number of hours worked in the week. For hours in excess of 40, the piece worker is entitled to be paid his piece rate earnings, plus a sum equivalent to one-half (not 1 ½) of this regular rate of pay multiplied by the number of hours worked in excess of 40 in the week.

See, 29 C.F.R. § 778.12 (day rate); 28 C.F.R. § 778.11 (piece rate).

6. COMMISSIONS

Commissions, regardless of the basis upon which they are calculated, and whether they are the sole source of income or given in addition to a guaranteed salary or hourly rate, must be included in the employee's regular rate. The fact that a commission is paid on some other basis than week, or that payment is delayed for a time past the employer's normal payday, does not excuse the employer from including the payment in the employee's regular rate.

If a commission is paid on a weekly basis it is added to the employee's other earnings for that workweek, and the total is divided by the total number of hours worked to obtain the employee's regular hourly rate. The employee must then be paid extra compensation at one-half of that rate for each hour worked in excess of 40 per week.

Overtime pay for employees paid wholly or partly on a commission basis may be computed on an "established basic rate," as set forth in federal regulations.

See, 29 C.F.R. § 778.117-118.

7. FIRE PROTECTION AND LAW ENFORCEMENT PERSONNEL

Overtime pay for police officers, firefighters and related employees may be determined on a 28-day work period rather than the 7-day workweek applied to other employees. The maximum number of hours that fire protection and law enforcement employees can work in the 28-day period without overtime is 212 and 171, respectively. These amounts are prorated for shorter work periods. Additionally, small government agencies have a complete overtime exemption with respect to fire protection and law enforcement employees if the agency employs less than five employees in fire protection or law enforcement activities during the workweek.

See, 29 U.S.C. § 207(k) and 29 C.F.R. §§ 553.210, 553.215; 25 U.S.C. § 213(b)(20).

C. DETERMINING TOTAL COMPENSATION

When calculating an employee's regular rate for the week, as a preliminary step, you must determine which such amounts must be factored into the equation when determining an employer's total compensation for the week.

1. PAYMENTS WHICH MUST BE INCLUDED

The FLSA defines the "regular rate" to broadly include "all remuneration for employment paid to, or on behalf of, the employee." Therefore, generally, you should assume that any amounts you pay to an employee based on his performance, productivity, or meeting certain work-related criteria or goals, must be included in the regular rate calculation. Here are examples of the kinds of payments which must typically be added into an employee's total compensation in order to determine the regular rate of pay: (a) Commissions; (b) Attendance bonuses; (c) Productivity bonuses; (d) Bonuses for quality or accuracy of work; (e) Shift differentials (such as premiums paid for hazardous work or night work); (f) Commissions; (g) Longevity pay; (h) Bonuses or other payments made pursuant to a contract, agreement, or promise (such as in a handbook or personnel policy); (i) Non-monetary awards (this includes the monetary value, meaning the cost to the employer, of any prize awarded to the employee for the quality, quantity, or efficiency of his work); (j) Voluntary overtime premiums, if the extra pay provided does not equal at least one and a half times the employee's regular hourly rate; (k) On-call pay, even if the employee does not work while on call.

2. DELAYED PAYMENTS

An interesting twist in the regular rate calculation arises when a commission, bonus, or other payment is paid irregularly, or cannot be identified with any particular workweek. Payments must be included in the overtime compensation determination, even if this means retroactively adjusting those computations once the amount of the bonus is determined. The commission or bonus is apportioned back over the workweeks of the period in which it was earned, with the employee being paid 1/2 the increase in the regular rate attributable to the bonus or commission.

If it is impossible to allocate such payments among workweeks in proportion to the amount of the payment actually earned each week, some other reasonable and equitable method of allocation must be adopted. For example, it may be reasonable and equitable to assume that the employee earned an equal amount of bonus each week of the period to which the bonus relates.

See, 29 C.F.R. § 778.109, 209(b)(bonuses); § 778.117-120 (deferred commissions).

3. AMOUNTS WHICH MAY BE EXCLUDED FROM THE REGULAR RATE

Certain types of compensation or remuneration may be excluded from the regular rate. All of these exclusions are based on specific statutory provisions or regulations. If a payment does not fit under one of these exclusions, it must be included in the regular rate: (a) Paid leave (such as holiday pay and sick pay) – however, you cannot credit paid leave against any overtime pay due to an employee; (b) Guaranteed pay for time not worked: (c) Reimbursement for mileage or other expenses; (d) Qualified payments for benefits, profit-sharing, and thrift or savings plans; (e) Sums paid as gifts, such as Christmas bonuses, given as a reward for service, but not based upon hours worked, production, or efficiency – unless this type of "gift" bonus is so large that employees count on it as part of their regular wages, or if it is made pursuant to an agreement or contract; (f) Extra compensation provided as a premium for an employee working in excess of his regularly scheduled hours or on weekends or holidays – IF such premium pay totals at least one and a half times the employee's regular hourly wage; (g) Bonuses that are based on a percentage of the employee's total earnings, *including overtime pay:* (h) Sums paid in recognition of services during a given period if both the fact that payment is to be made and the amount of the payment are determined at the sole discretion of

the employer at or near the end of the period, and not pursuant to any prior agreement or promise that such payments would be made.

Note there is an important distinction between whether a bonus payment is **discretionary** or **non-discretionary**.

See, 29 C.F.R. §§ 778.208-778.215.

4. CREDITS AGAINST OVERTIME

The FLSA does not require an employer to pay overtime twice for the same hours. Therefore, if you provide "premium pay" for long hours, holidays or weekend work, you may be entitled to credit some or all of that pay toward your overtime requirements under the FLSA.

If your premium pay policy sets a premium rate of at least one and a half times the employee's regular hourly rate, this premium pay may be excluded from your calculation of the employee's overtime, and credited towards your overtime obligations to the employee.

See, 29 C.F.R. §§ 778.207(h); 211(a); 212(a); 213; 214.

5. HOW DEDUCTIONS AFFECT THE REGULAR RATE

In general, the regular rate of an employee is computed without regard for deductions. For instance, if an employer makes deductions from an employee's weekly compensation based on the employer's cost for board and lodging, tools, or uniforms, or for disciplinary reasons, the regular rate is determined by dividing the employee's total compensation *before* deductions by the total hours worked in the workweek.

See, 29 C.F.R. §§ 778.305-307.

6. EXCEPTIONS TO THE REGULAR RATE PRINCIPLE

Under certain circumstances, an employer and an employee may reach a mutual agreement before work is commenced regarding a variation of the "regular rate." The circumstances are limited, and these contracts are subject to particular rules, regulations, and limitations. Some of these types of special agreements must be pre-approved by the United States Department of Labor. Such alternative pay arrangements include: (a) Paying an employee an "established rate" in lieu of the regular rate; (b) Providing "guaranteed compensation" in lieu of overtime compensation. This arrangement, called a "Belo contract," may only be used in occupations with duties which necessitate irregular work hours; (c) Pay employees pursuant to "piece rate contracts," which provide a simpler method of calculating overtime pay due to piece rate workers.

See, 29 U.S.C. § 207(g)(3); 29 C.F.R. Part 548 (Established rate); 29 C.F.R. §§ 404, 414(a)(Belo contracts); 29 U.S.C. § 207(g)(1) and (2)(Piece rate contracts).

IV. FLSA EXEMPTIONS

Certain categories of employees are exempt from the requirements we have been discussing so far. For these "exempt" employees, you do not need to track their time or pay overtime. However, exemptions from the overtime requirements of the FLSA are just that—exceptions to the rule. Exemptions are very narrowly construed, and you, as the employer, will always bear the burden of proving that you have correctly classified an employee as exempt.

Here are some common mistakes regarding FLSA exemptions: (a) "If I put an employee on salary, he becomes exempt.;" (b) "If an employee has a manager, supervisor, or administrator title, he is exempt."; (c) "If an employee is highly compensated, he is exempt."; (d) "If an employee is college-educated and performs white-collar office work, he is exempt."; (e) "If an employee has an advanced degree, he is exempt."; (f) "If an employee is performing inside sales work, he is exempt."; (g) "I have an employee who wants to be paid on salary, rather than hourly, and does not want to record his time. Based on his wishes, it is OK for me to treat him as exempt."; (h) "Everyone else in my industry classifies this position as exempt, therefore I am entitled to classify it as exempt."; (i) "The employees who I have classified as exempt don't work overtime, so it doesn't matter if I have misclassified them."

All of these assumptions are, simply, incorrect, and if you have classified employees as exempt on any of these bases, you need to look again.

See, 29 U.S.C. § 207(a)(1).

A. OVERVIEW OF FLSA EXEMPTIONS

1. WHITE COLLAR EXEMPTIONS

. The FLSA contains dozens of exemptions. However, the most well-known and commonly used are the so-called "white collar" exemptions for executive, administrative, and professional employees, as well as outside sales employees and computer professionals. Generally, in order to qualify for a white collar exemption, an employee must: (a) Perform duties which fit the FLSA's test for the exemption; and (b) Be paid at least $455 per week on a salary basis.

Again, an employee's duties are a critical factor in determining exempt status—merely paying an employee a salary and giving him an exempt-sounding job title are not enough to justify application of an exemption.

B. SALARIED BASIS OF PAYMENT

An employee is paid on a "salary basis" where, on a weekly or less frequent basis, the employee receives a predetermined amount of pay, which is not subject to reduction regardless of the quality or quantity of work. Further, the employee must receive the full salary for any week that she performs work without regard to the number of hours worked. An exempt employee's salary may only be subject to deductions in specific situations, as set forth in the regulations.

Here are some general rules for making sure you don't jeopardize the salaried basis of payment for an exempt employee: (a) Make sure the employee's pay is the same every week, regardless of the hours worked; (b) Use non-monetary means of disciplining exempt employees--avoid policies or practices of disciplining exempt employees for attendance or performance problems by docking their pay; (c) Never dock the pay of an exempt employee based on a partial day absence; (d) Make sure an exempt employee is paid for any day he's ready, willing, and able to work, and avoid policies or practices of making deductions based on lack of work.

Keep in mind that the salary basis rule is based upon the concept that exempt employees are not being paid for time worked, but, rather, for the value of services performed.

1. PERMISSIBLE DEDUCTIONS

Certain deductions are permissible. Deductions may be taken without jeopardizing exempt status only under the following circumstances: (a) When the employee has performed no work at all during the entire workweek; (b) When the employee is absent for a full day for personal reasons other than illness or disability (including a work related accident); (c) When the employee is absent for a full day where the deduction is made in accordance with a bona fide plan, policy or practice of providing compensation for loss of salary due to sickness, where the employee has not yet become eligible to participate in the plan or has exhausted all accrued leave allowed under the plan; (d) When an employee has violated a safety rule of major significance; (e) When an employee misses any work (whether a full day or partial day) due to taking leave under the Family and Medical Leave Act (FMLA); (f) When the employee is in the initial or terminal week of employment, an employer may pay a proportionate part of an employee's full salary for the time actually worked.

a. <u>Disciplinary Deductions</u>

Disciplinary deductions (i.e., suspensions without pay) of a full week are always permissible, so long as no work is performed in the week. For unpaid suspensions of less than a week, the employer must make sure that the suspension is imposed pursuant to a *written* disciplinary policy which is applicable to all employees.

b. <u>Absences due to business shutdowns</u>

The salary basis test is not satisfied where the employer makes deductions from the employees' predetermined compensation for "absences occasioned by...the operating requirements of the business."

See, 29 C.F.R. § 541.603-604.

2. PARTIAL DAY DEDUCTIONS

The regulations expressly state that, generally, even otherwise permissible deductions may only be made in increments of "one or more full days." In most instances, therefore, partial day deductions from the pay of exempt salaried employees are simply not allowed. Stated another way, ***if an exempt employee shows up for part of a workday, you must pay him for the whole day.***

a. <u>FMLA Leave</u>

There are a couple of exceptions to the prohibition against partial day pay deduction. First, an employer may deduct from an employee's salary for partial day absences if such absences constitute intermittent or reduced leave under the FMLA without losing the exempt status of the employee.

See, 29 C.F.R. § 825.206.

b. <u>Public Accountability</u>

There is another exception to the partial day deduction rule, when such deductions are made by public employers based on principles of "public accountability." This means that an otherwise exempt public sector employee does not lose his or her exempt status because the employer's pay system requires pay reductions for partial day absences taken for personal reasons or because of an illness when the employee does not use accrued leave. This applies to pay systems where accrued leave is not used because: (1) the employee does not seek permission to use the leave; (2) permission to use the leave is denied; (3) all accrued leave has been exhausted; or (4) the employee elects to use leave without pay. Additionally, **deductions** from the pay of an employee of a public agency for absences due to a budget-required furlough

shall not disqualify the employee from satisfying the salary basis test except in the week in which the furlough occurs.

See, 29 C.F.R. § 541.710.

3. DEDUCTIONS FROM PAID LEAVE

Deductions from paid leave do not impact exempt status. This includes partial day deductions. Remember, the FLSA does not regulate paid leave, only wages. So long as the employee's salary remains untouched, the exemption is safe.

See, 29 C.F.R. § 541.118(a)(3).

4. SAFE HARBOR PROVISION

There is a safe harbor provision. If you promptly reimburse the employee for the deduction, exempt status will remain intact. However, the safe harbor provision is available only to employers with a "clearly communicated policy" prohibiting improper pay deductions and the policy must contain a complaint mechanism. The best evidence of such a policy is a written policy distributed to employees at the time of hire, published in a handbook, or available on the company's intranet.

See, 29 C.F.R. § 541.118(a).

5. EFFECT OF ADDITIONAL PAYMENTS

Additional compensation, over and above the "predetermined amount," does not impact the employee's salaried status, even if that compensation comes in the form of pay at an hourly rate for each hour above the employee's regular schedule.

See, 29 C.F.R. § 541.118(b).

6. FEE FOR SERVICE PAYMENTS

The salary basis test includes compensation on a "fee basis." Accordingly, some employers pay their employees on a set fee per service basis, such as, in the publishing industry, a fixed rate for each article written or photograph taken. Under the regulations, if payment is at a rate that would exceed the statutory minimum if 40 hours were worked, then the employee may qualify for the exemption. However, the employer also must demonstrate that the fee payment is made for a job which is unique rather than for a series of jobs which are repeated an indefinite number of times and for which payment on an identical basis is made over and over again.

See, 29 C.F.R. § 541.313(b).

7. TIMEKEEPING FOR SALARIED EXEMPT EMPLOYEES

While employers are not required to track the time of an exempt employee, there is no prohibition against doing so. In other words, merely requiring an exempt, salaried employee to clock in and out will not destroy the exemption, so long as you don't make any deductions from his salary based on the amount of time worked.

8. EXEMPTIONS NOT SUBJECT TO SALARY REQUIREMENTS

Not all exemptions contain salary basis requirements. Here are the exceptions to that rule: (a) **Certain Licensed Professional Employees.** The compensation requirements do not apply to employees who hold a valid license or certificate permitting the practice of law (or medicine) and are actually engaged in such practice. This exception, however, does not apply to nurses, dietitians, etc. Thus, registered nurses who would otherwise qualify as exempt professional employees would still need to be paid on a salary basis at a rate of at least $455 a week; (b) **Computer Employees.** In the case of computer employees who are otherwise exempt based on the duties they perform, the salary requirements are met if they are paid a rate of not less than $27.43 an hour; (c) **Outside Sales Employees.** Employees meeting the requirements of the outside sales employee exemption are not subject to the salary requirements set forth herein.

C. EXECUTIVE EXEMPTION

An employee qualifies for the executive exemption if he: (1) Is compensated on a salary basis at a rate of not less than $455 per week; (2) Has a primary duty of management of the enterprise in which the employee is employed or of a customarily recognized department or subdivision thereof; (3) Customarily and regularly directs the work of two or more other employees; and (4) Has the authority to hire or fire other employees or whose suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees are given particular weight.

1. AREA OF RESPONSIBILITY

A management title alone doesn't make an employee an exempt executive. An exempt executive must truly be "in charge" of his designated area. He doesn't need to be entirely free from supervision—in other words, the fact that he must report to, and run some decisions by, a higher authority, will not jeopardize the exemption.

Factors a court will look at to determine whether an employee is truly an exempt manager include: (a) Whether he has unilateral authority to make at least some decisions of significance pertaining to his areas of responsibility (such as budgeting, ordering, personnel decisions, handling customer complaints, and maintenance of the facility); (b) How frequently he must report to his boss/how frequently his boss is physically present at the work site, and whether the boss effectively takes over the management function when present (c) Whether he is held accountable when his performance is assessed based upon successful operation of his area of responsibility; (d) Whether his pay is based in whole or in part upon successful operation of his area of responsibility.

2. PRIMARY DUTY OF MANAGEMENT

a. Management

> Federal regulations state that "management" includes activities such as: (a) Interviewing, selecting, and training employees; (b) Setting and adjusting employees' rates of pay and hours of work; (c) Directing the work of other employees; (d) Maintaining production or sales records for use in supervision or control of employees; (e) Appraising employees' productivity and efficiency for purposes of recommending promotions, demotions, terminations, or other changes in employment status; (f) Handling employee complaints and grievances; (g) Disciplining employees; and (h) Planning the work.

See, 29 C.F.R. § 541.102.

b. Primary Duty

"Primary duty" is defined for *all* exemptions (not just the executive exemption) as "the principal, main, major or most important duty that the employee performs." Factors that will be considered are: (a) The relative importance of the exempt duties compared to other duties; (b) The amount of time spent performing exempt work; (c) The employee's relative freedom from direct supervision; and (d) The relationship between the employee's salary and the wages paid to non-exempt employees who may be performing similar duties.

See, 29 C.F.R. § 541.700.

c. Working Supervisors

An employee may be exempt even if she performs exempt and non-exempt work at the same time, so long as the other parts of the executive exemption are met.

See, 29 C.F.R. § 541.106.

3. DIRECTION OF TWO OR MORE EMPLOYEES

"Two or more employees" means two or more full-time employees or their equivalent, such as one full-time employee and two part-time employees who together work 80 hours per week.

See, 29 C.F.R. § 541.104.

4. AUTHORITY TO MAKE PERSONNEL DECISIONS

To qualify as an exempt executive employee, a manager must have authority to hire, fire, or at least make recommendations regarding personnel decisions, which will be afforded significant weight by the employer.

A supervisor does not have to have unilateral authority to hire, fire, promote, set pay, or discipline employees, in order to meet this prong of the executive exemption. He just needs to play a role in the process, and be able to give recommendations on these issues, which are given some weight by the employer. If a supervisor does have such authority, be sure to indicate this in his job description.

See, 29 C.F.R. § 541.105.

D. ADMINISTRATIVE EXEMPTION

An employee qualifies for the executive exemption if he: (1) Is compensated on a salary or fee basis at a rate of not less than $455 per week; (2) Has a primary duty of performing office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and (3) Has a primary duty which includes the exercise of discretion and independent judgment with respect to matters of significance.

The administrative exemption is the most frequently misunderstood and misapplied exemption.

1. ADMINISTRATIVE WORK

First look to the nature of the work which he or she performs as his primary duty.

Performing "work related to the management or general business operations of the employer" generally means performing work which is linked with the running or servicing of the business. Such work must not be of a routine or clerical nature and must be of substantial importance to the management or operation of a business.

Another factor to consider is that "production" work is typically not exempt. Production work refers to any form of making or creating whatever product or service the employer offers for sale, or actually selling that product or service to the public.

Administrative work also includes work pertaining to "the management or the general business operations of the…employer's customers." Thus, employees who provide consultation and advice to an employer's clients may be considered to be performing exempt administrative work.

See, 29 C.F.R. § 541.201.

2. PRIMARY DUTY

As with the executive exemption, you must show that exempt work is the primary duty of an administrative employee. The fact that the employee performs some non-exempt work will not jeopardize the exemption. Again, the 50% rule is a useful guide in making this determination. Federal regulations expressly state that whether an employee's primary duty consists of exempt administrative work will be assessed based on all the facts of the case and "with the major emphasis on the character of the employee's job as a whole."

See, 29 C.F.R. § 541.700(a).

3. DISCRETION AND INDEPENDENT JUDGMENT

In order to qualify for the administrative exemption, it is not enough for an employee to have a primary duty consisting of exempt administrative work. He must also exercise discretion and judgment carrying out such duties. In general, independent judgment means that the employee compares and evaluates possible courses of action and makes a decision after considering the options.

The employee must have authority to make an independent choice, free from immediate direction or supervision. Even though her decision may be revised or reversed after review, she's still exercising independent judgment. However, the term means more than the use of a skill in applying well-established techniques, procedures, or specific standards described in manuals or other sources.

Non-exclusive, ten-factor test for determining if an employee exercises discretion and independent judgment with respect to matters of significance is often used. If the answer to any 2 or 3 of these factors is "yes," the employee will likely be found to exercise discretion and independent judgment with respect to matters of significance: (a) Whether the employee has authority to formulate, affect, interpret, or implement management policies or operating practices; (b) Whether the employee carries out major assignments in conducting the operations of the business; (c) Whether the employee performs work that affects business operations to a substantial degree, even if the employee's assignments are related to operation of a particular segment of the business; (d) Whether the employee has authority to commit the employer in matters that have significant financial impact; (e) Whether the employee has authority to waive or deviate from established policies and procedures without prior approval; (f) Whether the employee has authority to negotiate and bind the company on significant matters; (g) Whether the employee provides consultation or expert advice to management; (h) Whether the employee is involved in planning long- or short-term business objectives; (i) Whether the employee investigates and resolves matters of significance on behalf of

management; and (j) Whether the employee represents the company in handling complaints, arbitrating disputes or resolving grievances.

See, 29 C.F.R. § 541.202(b).

E. EDUCATION EMPLOYEES

There is a separate test (which is really a subcategory of the administrative exemption) for employees working at educational institutions. This test uses the same $455 salary requirement, and also requires that the employee's "primary duty consist of performing administrative functions directly related to academic instruction or training in an educational establishment or department or subdivision thereof." There is an additional section to the salary requirement that will not jeopardize the exemption if the employee makes less than $455, as long as he makes at least the entrance salary for teachers employed in the same educational establishment. This provision extends to principals, superintendents and other school administrators. Principals and vice-principals are included as examples in this section, while maintenance workers, dieticians, and school nurses are excluded, because their work does not directly relate to academic instruction or training.

See, 29 C.F.R. § 541.204.

F. PROFESSIONAL EXEMPTION

An exempt professional employee is one who: (1) Is compensated on a salary or fee basis at a rate of not less than $455 per week (except for certain licensed professionals in the fields of law and health care) and (2) Has a primary duty of the performance of work: (i) Requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction, or (ii) Requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

Thus, there are two very different types of professional exemptions—the learned professional and the creative professional.

See, 29 C.F.R. § 541.300.

1. LEARNED PROFESSIONALS

A learned professional performs work that usually involves analysis, interpretation or making deductions from facts and circumstances. The learned professional works with his intellect, not with his hands.

a. Fields of Learning

The types of learning fields covered by this exemption include: (a) Medicine; (b) Law; (c) Theology; (d) Accounting; (e) Actuarial computation; (f) Engineering; (g) Architecture; (h) Teaching; (i) Physical, chemical, and biological sciences; (j) Pharmacy; (k) Similar occupations.

b. Advanced Knowledge

A learned professional must have "advanced knowledge" in one of these fields. This is knowledge that is traditionally acquired through a prolonged course of specialized intellectual instruction. In other words, the more education the employee has, the more likely he may be deemed eligible for classification as

an exempt learned professional. Federal regulations specifically state that advanced knowledge can't be attained in high school but must ordinarily be attained through specialized academic training at a higher level. The regulations do not specify what "higher level" is required, but, suffice to say, the more secondary education an employee has, the more likely he will be deemed as qualifying for the exempt professional classification.

See, 29 C.F.R. §§ 300-301.

2. CREATIVE PROFESSIONALS

Work that is original and creative in character in a recognized field of artistic endeavor and the result of which depends primarily on the invention, imagination, or talent of the employee, is exempt creative work. It's difficult to assess the required qualifications for this exemption, since educational background isn't part of the test.

Generally, the following individuals are exempt creative professionals: (a) Actors; (b) Musicians, composers; (c) Artists who are given only general guidelines as to the subject matter; (d) Cartoonists who are given only the title or underlying concept for a cartoon; (e) Essayists, novelists, short-story writers and screenplay writers; (f) Writers in advertising agencies; (g) Journalists who contribute a unique interpretation or analysis to their work product, or who appear as on-air personalities, conduct interviews, or serve as narrators or commentators

See, 29 C.F.R. § 541.302.

G. OTHER EXEMPTIONS

1. EQUITY OWNERS

An exempt executive is any employee who owns at least a bona fide 20% equity interest in the enterprise in which he is employed, and who is actively engaged in its management. The salary basis test does not have to be met for this exemption.

See, 29 C.F.R. § 541.101.

2. COMPUTER PROFESSIONALS

To qualify for the computer occupations exemption, the employee must be one who is: (1) Compensated on a salary or fee basis at a rate of not less than $455 per week…exclusive of board, lodging or other facilities, or on an hourly basis at a rate not less than $27.63 an hour; and (2) Whose primary duty consists of: (a) The application of systems analysis techniques and procedures, including; (b) consulting with users, to determine hardware, software or system functional specifications; or (c) The design, development, documentation, analysis, creation, testing or; (d) modification of computer systems or programs, including prototypes, based on and related to user or system design specifications; or (e) the design, documentation, testing, creation or modification of computer programs related to machine operating systems; or (f) A combination of the aforementioned duties, the performance of which requires the same level of skills.

See, 29 C.F.R. § 541.400.

3. OUTSIDE SALES EMPLOYEES

The term "employee employed in the capacity of outside salesman" means any employee: (1)Whose primary duty is: (i) making sales within the meaning of section 3(k) of the Act, or (ii) obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and (2) Who is customarily and regularly engaged away from the employer's place or places of business in performing such primary duty.

When determining the primary duty of an outside sales employee, work performed "incidental to and in conjunction with" the employee's own outside sales or solicitations, including incidental deliveries and collections, counts as exempt work. Other work that furthers the employee's sales efforts also is regarded as exempt work including, for example, writing sales reports, updating or revising the employee's sales or display catalog, planning itineraries and attending sales conferences.

To qualify for this exemption, the employee must consummate the sale or make "direct efforts toward the consummation of a sale." Employees have a primary duty of making sales if they "obtain a commitment to buy" from the customer and are credited with the sale.

Work performed by phone or from an employee's home office is not exempt outside sales work, unless incidental to actual face-to-face, field-based selling.

See, 29 C.F.R. §§ 500-504.

4. COMMISSIONED SALES EMPLOYEES

An employee is exempt from the overtime requirements of the FLSA if he works for a retail or service establishment, his regular rate of pay is more than one and one-half the minimum wage and more than half of his compensation for a representative period (not less than one month) represents commissions on goods or services.

See, Under 29 U.S.C. § 207(i).

5. HIGHLY COMPENSATED EMPLOYEES

An employee paid more than $100,000 per year and who performs office or non-manual work will be considered exempt from overtime premiums if he has one identifiable executive, administrative, or professional duty that he customarily and regularly performs. The total annual compensation must include at least $455 per week paid on a salary or fee basis.

See, 29 C.F.R. § 541.601.

6. HOME HEALTH AIDES/DOMESTIC SERVICE EMPLOYEES

Employees engaged in domestic service employment are generally not covered by the overtime and minimum wage requirements of the FLSA. Regulations define domestic service employment as "services of a household nature performed by an employee in or about a private home (permanent or temporary) of the person by whom he or she is employed."

Exempt domestic services include companionship services, caring for ill, elderly, or mentally incapacitated patients. However, companionship services do not include services which are required to be performed by trained personnel, such as a registered nurse or a licensed practical nurse. Home health aides are not entitled to overtime pay under the FLSA. Home health aides provide companionship services and

perform duties which are often performed by nurses, but they do not qualify as "trained personnel" under the companionship services exemption of the FLSA.

This exemption includes employees providing companionship services to individuals in a private home, even if the employee is not directly employed by the patient, but is employed by a home health agency or other third party employer.

See, 29 C.F.R. § 552.

7. MOTOR CARRIER EXEMPTION

Under the Motor Carrier Act, employers do not have to pay overtime to "any employee with respect to whom the Secy. of Transportation has power to establish qualifications and maximum hours of service." An employee is subject to the Secretary of Transportation if his or her job involves operating a motor vehicle that transports goods in interstate commerce on public roadways.

See, 29 U.S.C. § 213(b).

South Carolina Bar
Continuing Legal Education Division

2018 SC BAR CONVENTION

Corporate, Banking & Securities Law Section

Friday, January 19

SBA Loans—An Overview

Sherwood M. Cleveland
Mallory Winter

SBA Loans – An Overview

SC Bar Convention

January 19, 2018

SBA History

- In the Small Business Act of **July 30, 1953**, Congress created the Small Business Administration, whose function was to "aid, counsel, assist and protect, insofar as is possible, the interests of small business concerns."; The charter also stipulated that SBA would ensure small businesses a "fair proportion"; of government contracts and sales of surplus property.
- From 1991 – 2017, SBA has originated **1.4 Million** loans in the amount of **$350 Billion** through the 7A program.
- 504 SBA Certified Development Company program as we know it today commenced in **1986**.
- Since 1990, approximately **158,000** CDC/504 loans have been closed and processed for nearly $84 Billion in debenture loans. Third party bank loans made in combination with these debentures bring the total to approximately **$210 Billion**

SBA Loan Eligibility

Size Standards	Businesses with tangible net worth less than $15MM and average net income after taxes for applicant and affiliates for the last two fiscal years of less than $5MM
Type of Business	For profit only Active Revenue – NO Real Estate Investments Franchises must be SBA approved
Location	Operations must be in the United States or possessions
Commercial Real Estate	Must be owner occupied (51% for existing structure)
Citizenship	US Citizen or Legal Permanent Resident (must be cleared by I.N.S.)
Repayment	Must be from business operations

Credit Elsewhere Test

- Borrower must be unable to obtain the loan under reasonable terms without a Federal Government Guarantee and financing is not available from resources of applicant's business.
- Factors demonstrating weakness in the applicant's credit or reflecting it would exceed Bank's loan limits include :
  - Business needs longer loan maturity than Bank can provide
  - Loan amount exceeds Bank's loan limit to a single customer
  - Collateral not meeting Bank's requirements
  - Bank's policy normally not allowing loans to new business or in this industry
- Unacceptable Factors include:
  - Meeting or addressing Bank's CRA compliance
  - Refinancing debt already on reasonable terms

Ineligible Businesses

- Banks
- Lenders or Investment Companies
- Life Insurance Companies
- Finance Companies
- Factors
- Investment Companies
- Bail Bond Companies
- Passive Businesses
  - Examples are Apartment Projects, Shopping Centers and Subdivision Residential nursing homes and assisted living facilities are eligible
- Life Insurance Companies
  - Agents may be eligible depending on level of control by the Life Insurance Company.
- Business located in Foreign Country or Owned by Illegal Alien
  - However, such are eligible if:
    - Located in U.S.
    - Operate primarily in U.S.
    - Authorized to operate in state or territory of operation
  - Make significant contribution to U.S. economy through payment of taxes or use of U.S. products, material or labor.

Other Ineligible Businesses

- Pyramid Selling Businesses
- Gambling (May be eligible if less than 1/3 of income from gambling)
- Illegal Activities
- Restricting Patronage
- Government Owned Entities
- Religious
- Co-operatives
- Loan Packaging
- Poor Character, Criminal Record, etc.
- Equity Interest by CDC
- Prurient Sexual Material
- Prior Loss to the Government
- Political/Lobbying Activities
- Speculation

7A Eligible Project Costs

- Acquiring Land and/or purchasing, constructing or renovating buildings
- Improving a site (e.g. grading, streets parking lots, landscaping, including up to 5% of the loan amount for community improvements such as curbs and sidewalks
- Acquiring and installing fixed assets
- Inventory
- Supplies
- Raw Materials (including work in progress)
- Working Capital
- Refinancing certain outstanding business debts
- Energy Conservation loans
- Change of Ownership/Business Acquisition

SBA 7A Loan Overview

- Maximum Loan Amount = $5,000,000
- Loan terms that exceed typical commercial lending
  - CRE – up to 25 years
  - Equipment – up to 10 years or useful life
  - Working Capital – up to 10 year term
- Lower equity injection
  - 0 – 10 % for CRE purchases for existing company
  - 0 – 10% for expansion
  - 10% for business acquisition
  - 0% for refinance
- No loan covenants or conditions required
- No balloons
- No prepayment if loan amortization is under 15 years; 15 years or more – Declining 3 year ppp - 5%, 3%, 1%

504 Purpose, Administration & Structure

- Purpose of 504 program is to encourage commercial lenders to provide loans to small businesses not otherwise able to obtain long term fixed rate financing on reasonable terms for the acquisition and/or construction of major fixed assets consisting of land, buildings, equipment and machinery. Purpose includes job creation and job retention.
  - One job must be created for every $65K of Debenture or $100K for small manufacturers. Job Retention Criteria can be used only if CDC can show jobs would be lost if project not done
- Administered through state nonprofit Certified Development Companies which are organized and structured to qualify as “certified” by SBA to participate in the administration of the 504 program as lenders.
- The CDC closes the 504 loan to Borrower(s) in its name and issues the Debenture, promising to pay to The Bank of New York, as Trustee, semi-annual payments which in turn fund payments to the investors, as certificate holders, who have purchased their interests in the debenture pool.
- The CDC Loan is assigned to the SBA which guarantees the payments under the Debentures, thus backed by the full faith and credit of the United States. Investors purchase interests in the debenture pool and receive certificates representing ownership of all or part of the pool.

SBA 504 Loan Overview

- Provides financing for long term assets ONLY (CRE and heavy equipment)
- No maximum loan amount on 1st mortgage. Maximum loan amount on debenture = $5,000,000 - $5,500,000
- Provides long term fixed rates for CDC loan portion (2nd mortgage)
  - CRE - 20 years fully amortizing with a fixed rate and 10 year prepayment penalty
  - Equipment and machinery- 10 years fully amortizing with a fixed rate and 5 year prepayment penalty
- Lower Equity Injection
  - 10% for existing business with multi-use of property
  - 15% for new business with multi-use property
  - 15% for existing business with special use property
  - 20% for new business with special use property
- Project assets are usually the only required collateral

504 Structure

Three Participants: Third Party Bank Lender providing 50% or greater of eligible project costs, CDC/SBA up to 40% and Borrower with at least 10% equity.

	Standard Structure	New Business **or** Special Purpose Prop	New Business **and** Special Purpose Prop.
Bank	At Least 50%	At Least 50%	At Least 50%
CDC/SBA	Max. of 40%	Max. of 35%	Max of 30%
Borrower	At Least 10%	At Least 15%	At Least 20%

Bank holds first priority lien of the Project assets financed and CDC has second lien backed by SBA's 100% SBA guaranteed Debenture. Borrower pays these loans separately to the Bank and to the CDC.

Borrower's Equity

- 100% of Borrower Equity must be injected prior to funding of Debenture and Banks should require Borrowers to inject 100% of their equity before funding any portion of Bank loan. Bank does have the option of funding commensurate with Borrower injections during construction.
- Borrower's equity in land previously acquired may be counted toward Borrower equity contribution, at cost if two years or less since Borrower acquired. If more than 2 years, at appraised value.
- Seller Purchase money financing of Project Property may qualify as portion of Borrower equity:
  - Interest Rate on Seller Note must be reasonable.
  - If loan secured by Project Property, it must be subordinate to the CDC's mortgage and may not be repaid at a faster rate than 504 loan.
  - Seller may not hold as security any voting rights or stock options in the Borrower.

504 Eligible Project Costs

- Land and Necessary Land Improvements (Grading, new streets, curbs, gutters, parking lots utilities, landscaping)
- If bought less than 2 years prior to application date, actual cost is the eligible project cost
- Building and Building Improvements
- Machinery and Equipment – Must have useful life of 10 years
- Furniture/Fixtures
- Professional Fees (not including attorney fees for closing of Bank or CDC loans)
- Borrower's expenditures for the above, Bridge Financing (max of 3 years) and Interim Financing – Points, Fees, Interest
- Contingency Fund – Not to exceed 10% of Project Construction Cost
- Permissible Debt Refinancing with Expansion (13CFR § 120.882(e)
  - SBA SOP 50 105(J) at Page 301 states: "If the Project involves expansion of an Applicant, any amount of existing indebtedness that does not exceed 50% of the costs of the expansion may be refinanced. The debt being refinanced will be added to the expansion cost to establish the total project costs, if all of the conditions discussed below are met. "Expansion" includes any project that involves the acquisition, construction or improvement of land, building or equipment for use by the Applicant." The twelve conditions required to be met for the refinancing to occur are listed on pages 302-304 of the SOP

Lawyer's Responsibility

- Whether you are serving as Counsel for Borrower or Lender, the legal approach to the transaction should be to treat the Bank part of the deal and the CDC part as component pieces of a single and coordinated transaction. If you are closing the Bank construction/acquisition loan, it is critical that the loan is prepared and closed, in all respects, in compliance with the terms and conditions of the SBA Debenture Authorization and the SBA SOP provisions relative to 504 transactions. The Bank may require that your opinion letter state and opine to that point.

Lawyer's Responsibility

- **Borrower(s) Entities.** The trend in these situations is to structure the Borrower as two separate entities, one as an Eligible Passive Company (EPC) and the other as an Operating Company (OC). The following are matters to address:
  - Articles of Incorporation or Organization.
  - Certificate(s) of Existence.
  - FEIN Letter(s) from IRS.
  - Signed Bylaws, Shareholder Management Agreement(s), Operating Agreement(s), Partnership Agreement(s).
  - Lease between EPC as Landlord and OC as Tenant which must be for term at least duration of the Debenture term and at a rental no greater than the carrying cost of the real estate - debt service of Bank and Debenture loans, ad valorem taxes, hazard insurance and reasonable maintenance and repairs.
- **Seller Transaction**
  - Certificate of Tax Compliance from Dept. of Revenue and Lien Search for UCC's,Tax Liens, Judgments, Bankruptcy filings
  - Seller Purchase Money Financing. If Seller and Borrower have agreed that Seller will provide a portion of the financing to constitute Borrower equity and to be secured by lien on Project Property subordinate to Bank and CDC, the Seller Note must be subject to Standby terms meeting SBA conditions to qualify the Seller financing as equity, including among other things that the Seller Note not be repaid at a faster rate than the Debenture and that Seller not undertake collection action without SBA consent.

Lawyer's Responsibility

- **Real Estate Title Issues.** As closing attorney on the Bank's acquisition/construction loan, it is imperative to consider whether there are title exceptions adversely affecting the appraised value and/or use of the real estate constituting the Project Property. In fact the SBA SOP in Subpart C, at Page 308, states:
  - "When assessing the adequacy of collateral the CDC must consider the impact that covenants and other restrictions recorded against the collateral may have on its value and marketability.... Examples of items to review include:
    - Deed restrictions, covenants, easement provisions, reversionary interests, subordinations, leases and options and other provisions that restrict the use of the property for the benefit of a third party....; and
    - Engineering Controls that require the small business concern or subsequent owners to install costly devices or structures such as extraction wells or subsurface barrier walls prior to constructing a building, remodeling, or otherwise improving the property. "

- **Survey Matters.** In a ground up construction project and in anticipation of the Debenture closing and funding post construction, it is essential to start with a good boundary survey which is either a Class A Urban Survey or, in complex/dense commercial areas, an ALTA survey which depicts on the plat how all easements restrictions, setbacks etc. affect the property. The same surveyor should be engaged to provide a foundation survey at that stage of the Project and an as-built survey at completion of the Project.

Lawyer's Responsibility

- **Certification(s) by Project Contractor, Architect and Engineer.** To comply with Debenture funding requirements, closing attorney on the acquisition/construction loan should have the above professionals certify that the building plans provide for a Project complying with all building codes and with seismic requirements as set forth in the SBA Debenture Authorization. Upon completion of the Project, the same persons should then certify to the Bank, CDC and SBA that the Project has been completed in accordance with said requirements.

- **Title Insurance Policy.** When the CDC Loan is closed and submitted to SBA District Counsel for funding approval, the title insurance policy must insure the CDC Mortgage and the assignment to SBA. Policy must show the Third Party Lender Agreement between Bank and CDC as an exception subsequent to the filed liens and, in the case of an EPC/OC Borrower structure, also show the lease related documents as subordinate exceptions. Title policy must also delete the arbitration clause from the policy.

Additional Products Offered

Product	Benefits	Who Qualifies	Max Loan	Use of Proceeds	Maturity	SBA Guaranty%
CAP Lines	• Working Capital – Revolving Line of Credit to meet cash flow cycles	US Citizens or LPR; For-profit businesses; meet SBA size standards; show good character, credit, management, and ability to repay.	$5M	•Working Capital • Advances Against Existing Inventory & A/R • Revolving LOC	**Generally:** • Up to 5 yrs.	75%
Export Working Capital Program	• Additional working capital to increase Export sales without disrupting domestic financing and business plans	US Citizens or LPR; For-profit businesses; meet SBA size standards; show good character, credit, management, and ability to repay. Plus, needs short term working capital for exporting.	$5M	• Working Capital •Transaction or asset based • Standby Letters of Credit	**Generally:** • 1 year or less • May go up to 3 yrs.	90% ($4.5MM maximum guarantee)
SBA Express	•Fast Turnaround •Streamlined Process •Easy-to-use Line of Credit	US Citizens or LPR; For-profit businesses; meet SBA size standards; show good character, credit, management, and ability to repay.	$350K	•Revolving Lines of Credit •Term Loan (same as 7(a))	**Generally:** •Revolving LOCs: Up to 7 years (inc. term out period) •M&E: up to 10 yrs. • Real Estate: 25 yrs. •Inventory up to 10 yrs.	50%
USDA	• Longer Terms • Fixed & Variable Rates •Proceeds develop and finance businesses in rural communities	Eligibility depends on the program and market. To check eligibility: **https://eligibility.sc.egov.usda.gov/eligibility/welcomeAction.do**	$10M	•Real Estate •Refinance • Construction •Expansion & Acquisition • Equipment Purchase • Partner Buyout •Franchise Financing	**Generally:** • Up to 30 yrs.	70% – 80%

Examples

Type of Industry/ Location: Automotive Upfit - SC

Loan Amount and Type: $1,125,000 7a

Overview:

- Company performs automotive upfits. The SBA loan was needed to purchase real estate.
- Loan request was challenging due to the business being in operation less than a year and limited liquidity of the guarantor.
- Loan ultimately approved based on past performance, projections supported by current job orders and the SBA guaranty.

Examples (cont.)

Type of Industry/ Location: Doctor - SC

Loan Amount and Type: $895,000 7a

Overview:

- Doctor had 20 years of experience and had been in the city for the past 10 years. Started solo practice 1 year before wanting to purchase commercial real estate.
- Loan request was challenging due to the business only being in operation for one year and limited liquidity of the guarantor.
- Loan ultimately approved based on current performance and projections, favorable industry and the SBA guaranty.

Examples (cont.)

Type of Industry/ Location: Restaurant – SC

Loan Amount and Type: $2,800,000 504 1st mortgage / $2,200,000 2nd mortgage and $120,000 Express LOC

Overview:

- Company is a start up restaurant. The SBA loan was needed for ground-up construction, FF&E and working capital.
- Loan request was challenging due to the business being a start-up and industry risk.
- Loan ultimately approved based on the direct industry management experience of the guarantor, financial strength of the guarantor and LTV after debenture funding.

Examples (cont.)

Type of Industry/ Location: Day Spa Franchise – SC

Loan Amount and Type: $2,789,000 7a and $125,000 Express LOC

Overview:

- Company is a start up day spa franchise. The SBA loan was needed to purchase real estate and FF&E.
- Loan request was challenging due to the business being a start-up and industry risk.
- Loan ultimately approved based on the strength of the franchise, financial strength of the guarantors and the SBA guaranty.

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South Carolina Bar
Continuing Legal Education Division

2018 SC BAR CONVENTION

Corporate, Banking & Securities Law Section

Friday, January 19

Ethics Update:
Including Opinion Practice and UPL

Mark S. Sharpe
Jennifer C. Blumenthal

MCNAIR

OPINION PRACTICE UPDATE: THE PROPOSED *STATEMENT OF OPINION PRACTICES*

STATEMENT OF OPINION PRACTICES [1]

WORKING DRAFT NOVEMBER 7, 2017

This version is published on the ABA Business Law Section Legal Opinions Committee website.
https://apps.americanbar.org/dch/committee.cfm?com=CL510000.

Note: This document has not been approved by the Joint Committee on Statement of Opinion Practices or its sponsoring organizations, the Board of the Working Group on Legal Opinions Foundation and the Legal Opinions Committee of the Business Law Section of the American Bar Association.

[1] This *Statement* has been published in *The Business Lawyer* [cite]. At the time of its publication, this *Statement* was approved by the bar associations and other lawyer groups identified in **Schedule I** (the "Schedule of Approving Organizations"). A current Schedule of Approving Organizations can be found at [URL]. Approval by a bar association or other lawyer group does not necessarily mean approval by individual members of that association or group.

{NOTE: The Corporate, Banking and Securities Law Section of the South Carolina Bar is an Approving Organization.}

STATEMENT OF OPINION PRACTICES

1. INTRODUCTION

Third-party legal opinion letters ("closing opinions")[2] are delivered at the closing of a business transaction by counsel for one party (the "opinion giver") to another party (the "opinion recipient") to satisfy a condition to the opinion recipient's obligation to close. A closing opinion includes opinions on specific legal matters ("opinions") and, in so doing, serves as a part of the diligence of the opinion recipient.[3]

This Statement of Opinion Practices (this "*Statement*") describes selected aspects of customary practice and other practices generally followed throughout the United States in the giving and receiving of closing opinions.[4]

[2] The terms "opinion letters" and "closing opinions" are commonly used to refer to third-party legal opinion letters, defined in this *Statement* as "closing opinions."

[3] References in this *Statement* to an opinion recipient mean the addressee of a closing opinion and any other person the opinion giver expressly authorizes to rely on the closing opinion.

[4] This *Statement* is drawn principally from: Comm. on Legal Op. of the Section of Bus. Law of the Am. Bar Ass'n, *Legal Opinion Principles,* 53 BUS. LAW. 831 (May 1998), and Comm. on Legal Op., *Guidelines for the Preparation of Closing Opinions,* 57 BUS. LAW. 875 (Feb. 2002). It updates the *Principles* in its entirety and selected provisions of the *Guidelines*. The other provisions of the *Guidelines* are unaffected, and no inference should be drawn from their omission from this *Statement*. Each provision of this *Statement* should be read and understood together with the other provisions of this *Statement*.

MCNAIR

STATEMENT OF OPINION PRACTICES

2. CUSTOMARY PRACTICE

Closing opinions and the opinions included in them are prepared and understood in accordance with the customary practice of lawyers who regularly give those opinions and lawyers who regularly review them for opinion recipients.[5] The phrase "customary practice" refers principally to the work lawyers are expected to perform to give opinions ("customary diligence") and the way certain words and phrases commonly used in closing opinions are understood ("customary usage"). Customary practice applies to a closing opinion whether or not the closing opinion refers to it or to this *Statement*.[6]

[5] *See Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions,* 63 BUS. LAW. 1277 (Aug. 2008) (the "*Customary Practice Statement*"), which has been approved by the bar associations and other lawyer groups listed at the end of that Statement and by additional groups following publication that can be found at [URL].

[6] *See infra* Section 10 (*Varying Customary Practice*).

STATEMENT OF OPINION PRACTICES

3. LEGAL OBLIGATIONS AND RULES OF PROFESSIONAL CONDUCT

When giving closing opinions, lawyers are subject to generally applicable legal obligations and to the rules governing the professional conduct of lawyers.[7]

[7] These include the duties opinion givers and counsel to opinion recipients owe to their own clients. [Counsel to opinion recipients also have duties to their clients, including duties relating to closing opinions.]

4. GENERAL

4.1 Expression of Professional Judgment

An opinion expresses the professional judgment of the opinion giver regarding the legal issues the opinion addresses. It is not a guarantee that a court will reach any particular result.

4.2. Bankruptcy Exception and Equitable Principles Limitation

The bankruptcy exception and equitable principles limitation apply to opinions even if they are not expressly stated.

4.3. Cost and Benefit

The benefit to the recipient of a closing opinion and of any particular opinion should warrant the time and expense required to give them.

STATEMENT OF OPINION PRACTICES

4.4. Golden Rule

Opinion givers and counsel for opinion recipients should be guided by a sense of professionalism and not treat closing opinions as if they were part of a business negotiation. An opinion giver should not be expected to give an opinion that counsel for the opinion recipient would not give in similar circumstances if that counsel were the opinion giver and had the requisite competence to give the opinion. Correspondingly, before declining to give an opinion it is competent to give, an opinion giver should consider whether a lawyer in similar circumstances would ordinarily give the opinion.

4.5. Reliance by Recipients

Opinion recipients are entitled to expect an opinion giver, in giving an opinion, to exercise the diligence customarily exercised by lawyers who regularly give that opinion.[8] In accepting a closing opinion, an opinion recipient ordinarily need not take any action to verify the opinions it contains. However, an opinion recipient is not entitled to rely on an opinion if it knows the opinion to be incorrect or if its reliance on the opinion is otherwise unreasonable under the circumstances.

[8] *See* the *Customary Practice Statement*. *See also infra* Section 10 (*Varying Customary Practice*).

4.6. Good Faith

An opinion giver and an opinion recipient and its counsel are each entitled to expect that the other is acting in good faith with respect to a closing opinion.

STATEMENT OF OPINION PRACTICES

5. FACTS AND ASSUMPTIONS

5.1. Reliance on Factual Information and Use of Assumptions

Because the lawyers preparing a closing opinion (the "opinion preparers") typically will not have personal knowledge of all the facts they need to support the opinions being given, they ordinarily are entitled to base those opinions on factual information provided by others, including their client, and on factual assumptions.

5.2. Reliance on Facts Provided by Others

An opinion giver is entitled to rely on factual information from an appropriate source unless the information appears irregular on its face or the opinion preparers know that the information is incorrect or know of facts that they recognize make their reliance under the circumstances otherwise unwarranted.

5.3. Scope of Inquiry Regarding Factual Matters

Opinion preparers are not expected to conduct an inquiry of other lawyers in their law firm or a review of the firm's records to ascertain factual matters, except to the extent they recognize that a particular lawyer is reasonably likely to have or a particular record is reasonably likely to contain information not otherwise known to them that they need to give an opinion.[9]

[9] References in this *Statement* to a law firm also apply to a law department of an organization.

STATEMENT OF OPINION PRACTICES

5.4. Reliance on Representations That Are Legal Conclusions

An opinion should not be based on a representation that is tantamount to the legal conclusion it expresses. An opinion may, however, be based on a legal conclusion in a certificate of an appropriate government official.

5.5. Factual Assumptions

Some factual assumptions on which opinions are based need to be stated expressly; others do not. Factual assumptions that ordinarily do not need to be stated expressly include assumptions of general application that apply regardless of the type of transaction or the nature of the parties. Examples are assumptions that copies of the documents are identical to the originals, signatures are genuine, the parties to the transaction other than the opinion giver's client (or a non-client whose obligations are covered by the opinion) have the power and have taken the necessary action to enter into the transaction, and the agreements those parties have entered into with the opinion giver's client (or the non-client) are enforceable against them. An opinion should not be based on an unstated assumption if the opinion preparers know that the assumption is incorrect or know of facts that they recognize make their reliance under the circumstances otherwise unwarranted. A stated assumption is not subject to this limitation because stating the assumption puts the opinion recipient on notice of the particular matters being assumed.[10]

[10] Basing an opinion on a stated assumption is subject to the generally applicable limitation described in Section 12 (*No Opinion That Will Mislead Recipient*).

STATEMENT OF OPINION PRACTICES

5.6. Limited Factual Confirmations and Negative Assurance

An opinion giver ordinarily should not be asked to confirm factual matters, even if the confirmation is limited to the knowledge of the opinion preparers. A confirmation of factual matters, for example, the accuracy of the representations and warranties in an agreement, does not involve the exercise of professional judgment by lawyers and therefore is not a proper subject for an opinion even when limited by a broadly-worded disclaimer. An exception is the confirmation sometimes requested regarding particular legal proceedings to which the client is a party. [11] Negative assurance regarding disclosures in a prospectus or other disclosure document may be provided in limited circumstances in connection with a sale of securities to assist the opinion recipient to establish a due diligence or similar defense.

[11] This *Statement* also applies, when appropriate in the context, to confirmations.

STATEMENT OF OPINION PRACTICES

6. LAW

6.1. Covered Law

When a closing opinion states that an opinion covers the law of a specific jurisdiction or particular laws, the opinion covers no other law or laws.

6.2. Applicable Law

An opinion on the law of a jurisdiction covers only the law of that jurisdiction that lawyers practicing in the jurisdiction, exercising customary diligence, would reasonably recognize as being applicable to the client or the transaction that is the subject of the opinion. A closing opinion does not cover some laws (for example, securities, tax and insolvency laws) that are otherwise applicable to the matters it addresses. A closing opinion also does not cover municipal and other local law. An opinion may, however, cover law that would not otherwise be covered if the closing opinion so states or the opinion does so expressly.[12]

[12] *See infra* Section 10 *(Varying Customary Practice)*.

STATEMENT OF OPINION PRACTICES

7. SCOPE

7.1. Matters Addressed

The opinions included in a closing opinion should be limited to reasonably specific and determinable matters of law that involve the exercise of professional judgment. A closing opinion covers only those matters it specifically addresses.

7.2. Matters Beyond the Expertise of Lawyers

Opinion givers should not be expected to give opinions on matters that are not within the expertise of lawyers (for example, financial statement analysis, economic forecasting and valuation). When an opinion depends on a matter not within the expertise of lawyers, an opinion giver may rely on information from an appropriate source or an express assumption with regard to the matter.

7.3. Relevance

Opinion requests should be limited to matters that are reasonably related to the opinion giver's client and the transaction that is the subject of the closing opinion. Depending on the circumstances, limiting assumptions, exceptions and qualifications to those reasonably related to the client, the transaction and the opinions given can facilitate the opinion process by making the closing opinion more informative.

STATEMENT OF OPINION PRACTICES

8. PROCESS

8.1. Opinion Recipient and Customary Practice

An opinion giver is entitled to presume that the opinion recipient is familiar with, or has obtained advice about, customary practice as it applies to the opinions it is receiving from the opinion giver.

8.2. Other Counsel's Opinion

Stating in a closing opinion reliance on an opinion of other counsel does not imply concurrence in the substance of that opinion. An opinion giver should not be expected to express concurrence in the substance of an opinion of other counsel.

8.3. Financial Interest in or Other Relationship with Client

Opinion preparers ordinarily do not attempt to determine whether others in their law firm have a financial interest in, or other relationship with, the client. Nor do they ordinarily disclose any such financial interest or other relationship that they or others in their firm have. If the opinion preparers recognize that such a financial interest or relationship exists, they should consider whether, even if disclosed, it will compromise their professional judgment with respect to the opinions being given.

STATEMENT OF OPINION PRACTICES

8.4. Client Consent and Disclosure of Information

If applicable rules of professional conduct require a client's consent to the delivery of a closing opinion, an opinion giver may infer that consent from a provision in the agreement making delivery a condition to closing or from other circumstances of the transaction. Unless a client gives its informed consent, an opinion giver should not give an opinion that discloses information the opinion preparers know the client would not want to be disclosed or as to which the opinion giver is otherwise subject to a duty of non-disclosure under applicable rules of professional conduct.

9. DATE

A closing opinion speaks as of its date. An opinion giver has no obligation to update a closing opinion for events or legal developments occurring after its date.

10. VARYING CUSTOMARY PRACTICE

The application of customary practice, including those aspects of customary practice described in this *Statement*, to a closing opinion or any particular opinion may be varied by a statement in the closing opinion or by an understanding with the opinion recipient or its counsel.

STATEMENT OF OPINION PRACTICES

11. RELIANCE

A closing opinion may be relied on only by its addressee and any other person the opinion giver expressly authorizes to rely. [13]

[13] This section does not address the circumstances in which reliance by others may be permitted as a matter of law. *See also supra* note 3.

12. NO OPINIONS THAT WILL MISLEAD RECIPIENT

An opinion giver should not give an opinion that the opinion preparers recognize will mislead the opinion recipient with regard to the matters it addresses. [14]

[14] As stated in *Third-Party "Closing" Opinions* by the TriBar Opinion Committee, 53 Bus. Law. 591, 603 (§1.4(d)) (Feb. 1998) (the "*TriBar Report*"), "[t]he question the opinion preparers must consider is whether under the circumstances the opinion will cause the opinion recipient to misevaluate the specific opinion given." The risk of misleading the opinion recipient can be avoided by appropriate disclosure. An opinion giver may limit the matters addressed by an opinion through the use of specific language (including a specific assumption, exception or qualification) so long as the opinion preparers do not recognize that the limitation itself will mislead the recipient. *See supra* Section 10 (*Varying Customary Practice*). **[Subject to Discussion]**

CORE OPINION PRINCIPLES

1. GENERAL
   - 1.1 *Customary Practice*.
   - 1.2 *Varying Customary Practice*.
   - 1.3 *Expression of Professional Judgment*.
   - 1.4 *Reliance by Recipients*.
   - 1.5 *Good Faith*.
   - 1.6 *Opinion Recipient and Customary Practice.*
   - 1.7 *Only Matters Specifically Addressed.*
   - 1.8 *Matters Beyond the Expertise of Lawyers*.
2. FACTS AND ASSUMPTIONS
   - 2.1 *Reliance on Factual Information and Use of Assumptions.*
   - 2.2 *Reliance on Facts Provided by Third Parties.*
   - 2.3 *Scope of Inquiry.*
   - 2.4 *Reliance on Representations That Are Legal Conclusions.*
   - 2.5 *Factual Assumptions.*
3. LAW
   - 3.1 *Covered Law.*
   - 3.2 *Applicable Law*.
4. MISCELLANEOUS
   - 4.1 *Date.*
   - 4.2 *Reliance*.

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QUESTIONS?

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2018 South Carolina Bar Convention
Corporate, Banking and Securities Law Section

OPINION PRACTICE UPDATE:
The Proposed Statement of Opinion Practices

A. Third-Party Opinions – In General. Lawyers are frequently asked to deliver legal opinions in a variety of business, corporate and commercial transactions to third parties who are not the lawyer's client in the transaction. These opinions are provided by the lawyer as counsel to an obligor in the transaction in the form of an opinion letter delivered to the non-client third party at the closing of the transaction (referred to as a "closing" or "third-party" legal opinion). The opinion is requested as part of the recipient's due diligence and forces the opinion giver to perform the necessary due diligence to ensure that the requisite legal formalities have been met.

B. The South Carolina Legal Opinion Report. Many state and national legal associations have adopted various opinion reports and guidelines to assist lawyers in the preparation of legal opinions. In South Carolina, an opinion preparer may rely the South Carolina Third-Party Legal Opinion Report (the "Report") of the Legal Opinion Ad Hoc Committee (the "Committee") of the Corporate, Banking and Securities Law Section (the "Section") of the South Carolina Bar.[1] The Report (i) provides guidance to South Carolina attorneys in preparing third-party legal opinions, (ii) establishes and defines acceptable opinion practices in the state, (iii) identifies opinion issues specific to state law and practices, (iv) confirms customary opinion practice in the state, and (v) adopts certain national guidelines governing opinion practice. The Report addresses state-specific issues and ethical considerations, including issues faced by South Carolina attorneys acting as local counsel in multi-state transactions. The Report relies on existing reports of the ABA and TriBar opinion committees, on nationally recognized opinion treatises, and on specific state statutes and case law for support.

The Report opens with an annotated illustrative form of opinion, which has been widely accepted and is currently in use by many practitioners in the state. Following the illustrative form, the Report includes ten sections covering opinion topics in greater detail. Part VI goes into detail on real estate related opinions and includes a discussion of the unauthorized practice of law (UPL) in relation to mortgage opinions, including ethical considerations and the impact on enforceability. While UPL is not typically addressed in a closing opinion, a stated assumption that there has been no unauthorized practice of law in the transaction is customary in South Carolina. Notwithstanding that assumption, a South Carolina opinion giver should consider whether any unauthorized practice of law is implicated in the transaction, both from an ethical standpoint and from a substantive enforceability standpoint (whether a note and mortgage could be deemed unenforceable as a result of any associated UPL). The opinion giver should not give the opinion if the opinion preparer has actual knowledge that any unauthorized practice of law has occurred. These issues appear to be unique to South Carolina.

[1] The Report was approved by the House of Delegates on January 22, 2015 and is posted on the South Carolina Bar's website at https://www.scbar.org/media/filer_public/61/e4/61e4a4ae-ff43-43f4-bf1f-a8238f711c72/corporate_third_party_legal_report.pdf.

C. Customary Practice. As a starting point, opinions in the state should be requested and rendered in accordance with "customary practice" and should attempt to follow the general language and guidelines set forth in the Report, including the Illustrative Form of Opinion. The Section approved the *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions*, 63 Bus. Law. 1277 (Aug. 2008), and all opinions in the state should be rendered in accordance with customary practice as set forth therein. A lawyer rendering, requesting and negotiating legal opinions should be familiar with the nationally recognized reports and guidelines and evolving trends in customary practice. Usually, attorneys familiar with customary practice will not pressure opinion givers for questionable or inappropriate opinions once a reasonable objection has been made. If the opinion request is inconsistent with the customary practice, the opinion should not be given, and an attorney familiar with customary opinion practice will not unduly pursue it.

D. Proposed Draft Statement of Opinion Practices. Since the publication of the *Statement on the Role of Customary Practice*, the ABA Business Law Section Legal Opinion Committee and the Working Group on Legal Opinions have undertaken a joint project to update the understanding of customary practice. As a result of that project, the Joint Committee on the Statement of Opinion Practices (the "Joint Committee") prepared drafts of the *Statement of Opinion Practices* ("Statement") and the *Core Opinion Principles* ("Principles"). The purpose of the Statement is to update the understanding of "customary practice," as agreed by attorneys who routinely give and request third-party legal opinions. The Principles summarize some of the key principles taken from the Statement and will replace the ABA *Legal Opinion Principles*, 53 Bus. Law. 831 (1998). The Principles are intended to be referenced or incorporated in opinion letters. The Statement and the Principles amplify, but do not replace, the *Statement on the Role of Customary Practice*. The Joint Committee has been working to reach consensus on the Statement and has requested the approval of the Statement and Principles by other bar associations and lawyer groups. Working drafts of the Statement and Principles were approved by the Section Council on May 24, 2017, and by the Board of Governors on July 20, 2017, subject to final approval by the Joint Committee. The working draft of the Statement, as of November 7, 2017, is attached hereto as Exhibit A, and the April 7, 2017 working draft of the Principles is attached hereto as Exhibit B.[2]

The following is a brief summary of the opinion practice statements addressed by the Statement and the outline of the Principles. The number in bold brackets at the end of each statement is the corresponding section in the Principles. (Please refer to the corresponding section references of the Statement and the Principles attached hereto for the exact wording.)

THE STATEMENT OF OPINION PRACTICES (summary)

1. INTRODUCTION – The Introduction discusses the meaning and purpose of closing opinions and identifies certain aspects of opinion practice that are generally followed throughout the United States in connection with rendering closing opinions.

[2] Current drafts of the Statement and Principles are available under "Discussion Documents" on the ABA Legal Opinions Committee website at https://apps.americanbar.org/dch/committee.cfm?com=CL510000.

2. CUSTOMARY PRACTICE – Closing opinions are prepared and understood in accordance with customary practice. "Customary practice" is the practice of lawyers who regularly give and review closing opinions and refers to the due diligence lawyers are expected to perform to give opinions ("customary diligence") and the meaning of certain words and phrases commonly used in closing opinions ("customary usage"). **[1.1]**

3. LEGAL OBLIGATIONS AND RULES OF PROFESSIONAL CONDUCT – Lawyers are subject to generally applicable legal obligations and to the Rules of Professional Conduct in rendering and reviewing legal opinions, including the duties owed to the lawyers' own clients.

4. GENERAL **[1]**

4.1 *Expression of Professional Judgment* – An opinion is not a guarantee of any outcome. **[1.3]**

4.2 *Bankruptcy Exception and Equitable Principles Limitation* – These qualifications apply to all opinions, whether expressly stated or not.

4.3 *Cost and Benefit* – The time and cost to render an opinion should not exceed the benefit to the recipient.

4.4 *Golden Rule* – Lawyers should adhere to their duty of professionalism. A lawyer should not ask for an opinion the lawyer would not give or refuse to give an opinion ordinarily given.

4.5 *Reliance by Recipients* – A recipient may not rely on an opinion it knows is incorrect or if reliance under the circumstances is unreasonable. **[1.4]**

4.6 *Good Faith* – The parties are expected to act in good faith. **[1.5]**

5. FACTS AND ASSUMPTIONS **[2]**

5.1 *Reliance on Factual Information and Use of Assumptions* – Lawyers rendering opinions may rely on factual assumptions. **[2.1]**

5.2 *Reliance on Facts Provided by Third Parties* – Lawyers rendering opinions may rely on facts by others unless known to be false. **[2.2]**

5.3 *Scope of Inquiry* – An opinion giver is not expected to conduct an in depth inquiry of files or others, unless a particular lawyer is known to have information. **[2.3]**

5.4 *Reliance on Representations That Are Legal Conclusions* – A lawyer rending an opinion should not rely on such representations. However, an opinion may be based on legal conclusions set forth in a governmental certificate. **[2.4]**

5.5 *Factual Assumptions* – Some assumptions are implied; others should be expressly stated. An opinion may not be based on an unstated assumption if the lawyer knows facts to the contrary. An opinion may not be based on a stated assumption if the opinion is misleading. **[2.5]**

5.6 *Limited Factual Confirmations and Negative Assurance* – A lawyer should not be asked to confirm facts, even if limited to the lawyer's knowledge. Negative assurance is limited to disclosures in connection with the sale of securities.

6. LAW **[3]**

6.1 *Covered Law* – No law is covered by an opinion other than the law of the jurisdiction expressly stated. **[3.1]**

6.2 *Applicable Law* – Only the law of the jurisdiction that is reasonably recognized as being applicable, exercising customary due diligence, is covered. Certain laws, such as securities, tax, insolvency and municipal law, are excluded. **[3.2]**

7. SCOPE

7.1 *Matters Addressed* – Opinions are limited to specific matters of law involving the exercise of professional judgment. **[1.7]**

7.2 *Matters Beyond the Expertise of Lawyers* – Lawyers are not be expected to give opinions beyond legal matters. **[1.8]**

7.3 *Relevance* – An opinion request should be limited to matters that are reasonably related to the client and the transaction.

8. PROCESS

8.1 *Opinion Recipient and Customary Practice* – An opinion giver can assume the recipient is familiar with customary practice. **[1.6]**

8.2 *Other Counsel's Opinion* – An opinion giver is not expected to concur with another counsel's opinion.

8.3 *Financial Interest in or Other Relationship with Client* – Such information is not required to be determined or disclosed. However, if such interest or relationship exists, the lawyer must determine whether the lawyer's professional judgment is impaired as a result.

8.4 *Client Consent and Disclosure of Information* – Client consent is inferred from the condition for a closing opinion. However, an opinion giver cannot disclose client confidential information without informed consent.

9. DATE – A closing opinion speaks as of its date. There is no obligation to update for subsequent events. **[4.1]**

10. VARYING CUSTOMARY PRACTICE – Customary practice may be varied by a statement in the opinion or by an understanding with recipient or its counsel. **[1.2]**

11. RELIANCE – Only the addressee and those expressly authorized may rely on the opinion. **[4.2]**

12. NO OPINIONS THAT WILL MISLEAD RECIPIENT – A lawyer may not give an opinion that the lawyer recognizes will be misleading with respect to the matter the opinion intends to address.

CORE OPINION PRINCIPLES (table of contents)

Exhibit A

[Working Draft dated November 7, 2017. This document has not been approved by the Joint Committee on Statement of Opinion Practices or its sponsoring organizations, the Board of the Working Group on Legal Opinions Foundation and the American Bar Association's Legal Opinions Committee]

STATEMENT OF OPINION PRACTICES[1]

1 INTRODUCTION

Third-party legal opinion letters ("closing opinions") [2] are delivered at the closing of a business transaction by counsel for one party (the "opinion giver") to another party (the "opinion recipient") to satisfy a condition to the opinion recipient's obligation to close. A closing opinion includes opinions on specific legal matters ("opinions") and, in so doing, serves as a part of the diligence of the opinion recipient. [3]

This Statement of Opinion Practices (this "*Statement*") describes selected aspects of customary practice and other practices generally followed throughout the United States in the giving and receiving of closing opinions. [4]

2 CUSTOMARY PRACTICE

Closing opinions and the opinions included in them are prepared and understood in accordance with the customary practice of lawyers who regularly give those opinions and lawyers who regularly review them for opinion

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[1] This *Statement* has been published in *The Business Lawyer* [cite]. At the time of its publication, this *Statement* was approved by the bar associations and other lawyer groups identified in **Schedule I** (the "Schedule of Approving Organizations"). A current Schedule of Approving Organizations can be found at [URL]. Approval by a bar association or other lawyer group does not necessarily mean approval by individual members of that association or group.

[2] The terms "opinion letters" and "closing opinions" are commonly used to refer to third-party legal opinion letters, defined in this *Statement* as "closing opinions."

[3] References in this *Statement* to an opinion recipient mean the addressee of a closing opinion and any other person the opinion giver expressly authorizes to rely on the closing opinion.

[4] This *Statement* is drawn principally from: Comm. on Legal Op. of the Section of Bus. Law of the Am. Bar Ass'n, *Legal Opinion Principles,* 53 BUS. LAW. 831 (May 1998), and Comm. on Legal Op., *Guidelines for the Preparation of Closing Opinions,* 57 BUS. LAW. 875 (Feb. 2002). It updates the *Principles* in its entirety and selected provisions of the *Guidelines*. The other provisions of the *Guidelines* are unaffected, and no inference should be drawn from their omission from this *Statement*. Each provision of this *Statement* should be read and understood together with the other provisions of this *Statement*.

recipients.[5] The phrase "customary practice" refers principally to the work lawyers are expected to perform to give opinions ("customary diligence") and the way certain words and phrases commonly used in closing opinions are understood ("customary usage"). Customary practice applies to a closing opinion whether or not the closing opinion refers to it or to this *Statement*.[6]

3 LEGAL OBLIGATIONS AND RULES OF PROFESSIONAL CONDUCT

When giving closing opinions, lawyers are subject to generally applicable legal obligations and to the rules governing the professional conduct of lawyers.[7]

4 GENERAL

4.1 Expression of Professional Judgment

An opinion expresses the professional judgment of the opinion giver regarding the legal issues the opinion addresses. It is not a guarantee that a court will reach any particular result.

4.2 Bankruptcy Exception and Equitable Principles Limitation

The bankruptcy exception and equitable principles limitation apply to opinions even if they are not expressly stated.

4.3 Cost and Benefit

The benefit to the recipient of a closing opinion and of any particular opinion should warrant the time and expense required to give them.

4.4 Golden Rule

Opinion givers and counsel for opinion recipients should be guided by a sense of professionalism and not treat closing opinions as if they were part of a business negotiation. An opinion giver should not be expected to give an opinion that counsel for the opinion recipient would not give in similar circumstances if that counsel were the opinion giver and had the requisite competence to give the opinion. Correspondingly, before declining to give

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[5] *See Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions,* 63 BUS. LAW. 1277 (Aug. 2008) (the "*Customary Practice Statement*"), which has been approved by the bar associations and other lawyer groups listed at the end of that Statement and by additional groups following publication that can be found at [URL].

[6] *See infra* Section 10 (*Varying Customary Practice*).

[7] These include the duties opinion givers and counsel to opinion recipients owe to their own clients.

an opinion it is competent to give, an opinion giver should consider whether a lawyer in similar circumstances would ordinarily give the opinion.

4.5 Reliance by Recipients

Opinion recipients are entitled to expect an opinion giver, in giving an opinion, to exercise the diligence customarily exercised by lawyers who regularly give that opinion.[8] In accepting a closing opinion, an opinion recipient ordinarily need not take any action to verify the opinions it contains. However, an opinion recipient is not entitled to rely on an opinion if it knows the opinion to be incorrect or if its reliance on the opinion is otherwise unreasonable under the circumstances.

4.6 Good Faith

An opinion giver and an opinion recipient and its counsel are each entitled to expect that the other is acting in good faith with respect to a closing opinion.

5 FACTS AND ASSUMPTIONS

5.1 Reliance on Factual Information and Use of Assumptions

Because the lawyers preparing a closing opinion (the "opinion preparers") typically will not have personal knowledge of all the facts they need to support the opinions being given, they ordinarily are entitled to base those opinions on factual information provided by others, including their client, and on factual assumptions.

5.2 Reliance on Facts Provided by Others

An opinion giver is entitled to rely on factual information from an appropriate source unless the information appears irregular on its face or the opinion preparers know that the information is incorrect or know of facts that they recognize make their reliance under the circumstances otherwise unwarranted.

5.3 Scope of Inquiry Regarding Factual Matters

Opinion preparers are not expected to conduct an inquiry of other lawyers in their law firm or a review of the firm's records to ascertain factual matters, except to the extent they recognize that a particular lawyer is reasona-

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[8] *See* the *Customary Practice Statement*. *See also infra* Section 10 (*Varying Customary Practice*).

bly likely to have or a particular record is reasonably likely to contain information not otherwise known to them that they need to give an opinion.[9]

5.4 Reliance on Representations That Are Legal Conclusions

An opinion should not be based on a representation that is tantamount to the legal conclusion it expresses. An opinion may, however, be based on a legal conclusion in a certificate of an appropriate government official.

5.5 Factual Assumptions

Some factual assumptions on which opinions are based need to be stated expressly; others do not. Factual assumptions that ordinarily do not need to be stated expressly include assumptions of general application that apply regardless of the type of transaction or the nature of the parties. Examples are assumptions that copies of the documents are identical to the originals, signatures are genuine, the parties to the transaction other than the opinion giver's client (or a non-client whose obligations are covered by the opinion) have the power and have taken the necessary action to enter into the transaction, and the agreements those parties have entered into with the opinion giver's client (or the non-client) are enforceable against them. An opinion should not be based on an unstated assumption if the opinion preparers know that the assumption is incorrect or know of facts that they recognize make their reliance under the circumstances otherwise unwarranted. A stated assumption is not subject to this limitation because stating the assumption puts the opinion recipient on notice of the particular matters being assumed.[10]

5.6 Limited Factual Confirmations and Negative Assurance

An opinion giver ordinarily should not be asked to confirm factual matters, even if the confirmation is limited to the knowledge of the opinion preparers. A confirmation of factual matters, for example, the accuracy of the representations and warranties in an agreement, does not involve the exercise of professional judgment by lawyers and therefore is not a proper subject for an opinion even when limited by a broadly-worded disclaimer. An exception is the confirmation sometimes requested regarding particular legal proceedings to which the client is a party.[11] Negative assurance regarding

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[9] References in this *Statement* to a law firm also apply to a law department of an organization.

[10] Basing an opinion on a stated assumption is subject to the generally applicable limitation described in Section 12 (*No Opinion That Will Mislead Recipient*).

[11] This *Statement* also applies, when appropriate in the context, to confirmations.

disclosures in a prospectus or other disclosure document may be provided in limited circumstances in connection with a sale of securities to assist the opinion recipient to establish a due diligence or similar defense.

6 LAW

6.1 Covered Law

When a closing opinion states that an opinion covers the law of a specific jurisdiction or particular laws, the opinion covers no other law or laws.

6.2 Applicable Law

An opinion on the law of a jurisdiction covers only the law of that jurisdiction that lawyers practicing in the jurisdiction, exercising customary diligence, would reasonably recognize as being applicable to the client or the transaction that is the subject of the opinion. A closing opinion does not cover some laws (for example, securities, tax and insolvency laws) that are otherwise applicable to the matters it addresses. A closing opinion also does not cover municipal and other local law. An opinion may, however, cover law that would not otherwise be covered if the closing opinion so states or the opinion does so expressly. [12]

7 SCOPE

7.1 Matters Addressed

The opinions included in a closing opinion should be limited to reasonably specific and determinable matters of law that involve the exercise of professional judgment. A closing opinion covers only those matters it specifically addresses.

7.2 Matters Beyond the Expertise of Lawyers

Opinion givers should not be expected to give opinions on matters that are not within the expertise of lawyers (for example, financial statement analysis, economic forecasting and valuation). When an opinion depends on a matter not within the expertise of lawyers, an opinion giver may rely on information from an appropriate source or an express assumption with regard to the matter.

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[12] *See infra* Section 10 *(Varying Customary Practice)*.

7.3 Relevance

Opinion requests should be limited to matters that are reasonably related to the opinion giver's client and the transaction that is the subject of the closing opinion. Depending on the circumstances, limiting assumptions, exceptions and qualifications to those reasonably related to the client, the transaction and the opinions given can facilitate the opinion process by making the closing opinion more informative.

8 PROCESS

8.1 Opinion Recipient and Customary Practice

An opinion giver is entitled to presume that the opinion recipient is familiar with, or has obtained advice about, customary practice as it applies to the opinions it is receiving from the opinion giver.

8.2 Other Counsel's Opinion

Stating in a closing opinion reliance on an opinion of other counsel does not imply concurrence in the substance of that opinion. An opinion giver should not be expected to express concurrence in the substance of an opinion of other counsel.

8.3 Financial Interest in or Other Relationship with Client

Opinion preparers ordinarily do not attempt to determine whether others in their law firm have a financial interest in, or other relationship with, the client. Nor do they ordinarily disclose any such financial interest or other relationship that they or others in their firm have. If the opinion preparers recognize that such a financial interest or relationship exists, they should consider whether, even if disclosed, it will compromise their professional judgment with respect to the opinions being given.

8.4 Client Consent and Disclosure of Information

If applicable rules of professional conduct require a client's consent to the delivery of a closing opinion, an opinion giver may infer that consent from a provision in the agreement making delivery a condition to closing or from other circumstances of the transaction. Unless a client gives its informed consent, an opinion giver should not give an opinion that discloses information the opinion preparers know the client would not want to be disclosed or as to which the opinion giver is otherwise subject to a duty of nondisclosure under applicable rules of professional conduct.

9 DATE

A closing opinion speaks as of its date. An opinion giver has no obligation to update a closing opinion for events or legal developments occurring after its date.

10 VARYING CUSTOMARY PRACTICE

The application of customary practice, including those aspects of customary practice described in this *Statement*, to a closing opinion or any particular opinion may be varied by a statement in the closing opinion or by an understanding with the opinion recipient or its counsel.

11 RELIANCE

A closing opinion may be relied on only by its addressee and any other person the opinion giver expressly authorizes to rely.[13]

12 NO OPINIONS THAT WILL MISLEAD RECIPIENT

An opinion giver should not give an opinion that the opinion preparers recognize will mislead the opinion recipient with regard to the matters it addresses.[14]

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[13] This section does not address the circumstances in which reliance by others may be permitted as a matter of law. *See also supra* note 3.

[14] As stated in *Third-Party "Closing" Opinions* by the TriBar Opinion Committee, 53 Bus. Law. 591, 603 (§1.4(d)) (Feb.1998) (the "*TriBar Report*"), "[t]he question the opinion preparers must consider is whether under the circumstances the opinion will cause the opinion recipient to misevaluate the specific opinion given." The risk of misleading the opinion recipient can be avoided by appropriate disclosure. An opinion giver may limit the matters addressed by an opinion through the use of specific language (including a specific assumption, exception or qualification) so long as the opinion preparers do not recognize that the limitation itself will mislead the recipient. *See supra* Section 10 (*Varying Customary Practice*). **[Subject to Discussion]**

Exhibit B

[As approved by the Joint Committee on Statement of Opinion Practices on March 28, 2017 and by the Legal Opinions Committee of the American Bar Association's Business Law Section on April 7, 2017, subject to approval by the Board of Directors of the Working Group on Legal Opinions Foundation]

CORE OPINION PRINCIPLES

The following *Core Opinion Principles* are drawn from the *Statement of Opinion Practices,* ___ BUS. LAW. ___ ( ) (the "*Statement*"), and are intended to have the same meaning as the provisions of the *Statement* from which they are drawn. The *Statement*, which has been approved by the bar associations and other lawyer groups identified in Schedule I to the *Statement*, describes selected aspects of customary practice and other practices followed throughout the United States in the giving and receiving of closing opinions. In doing so, it amplifies the *Statement on the Role of Customary Practice in the Preparation and Understanding of Third-Party Legal Opinions*, 63 BUS. LAW. 1277 (Aug. 2008). The *Core Opinion Principles* are designed for use by opinion givers (both law firms and law departments of organizations) who wish to incorporate or attach to their opinion letters a more concise statement of some of the opinion principles included in the *Statement*.

CORE OPINION PRINCIPLES

1. General

1.1 *Customary Practice.* Third-party legal opinion letters given at the closing of a business transaction ("closing opinions") by counsel for one party (the "opinion giver") to another party (the "opinion recipient," which term includes any other person expressly authorized to rely on the closing opinion) are prepared and understood in accordance with the customary practice of lawyers who regularly give them and lawyers who regularly review them for opinion recipients. The phrase "customary practice" refers principally to the work lawyers are expected to perform to give the opinions included in a closing opinion and the way certain words and phrases commonly used in closing opinions are understood.

1.2 *Varying Customary Practice.* The application of customary practice to a closing opinion or a particular opinion may be varied by a statement in the closing opinion or the opinion or by an understanding with the opinion recipient or its counsel.

1.3 *Expression of Professional Judgment.* An opinion expresses the professional judgment of the opinion giver regarding the legal issues the opinion addresses. It is not a guarantee that a court will reach any particular result.

1.4 *Reliance by Recipients.* In accepting a closing opinion, an opinion recipient ordinarily need not take any action to verify the opinions it contains. However, an opinion recipient is not entitled to rely on an opinion if it knows the opinion to be incorrect or if its reliance on the opinion is otherwise unreasonable under the circumstances.

1.5 *Good Faith.* An opinion giver and an opinion recipient and its counsel are each entitled to expect that the other is acting in good faith with respect to a closing opinion.

1.6 *Opinion Recipient and Customary Practice.* An opinion giver is entitled to presume that the opinion recipient is familiar with, or has obtained advice about, customary practice as it applies to the opinions it is receiving from the opinion giver.

1.7 *Only Matters Specifically Addressed.* A closing opinion covers only those matters it specifically addresses.

1.8 *Matters Beyond the Expertise of Lawyers.* Opinion givers should not be expected to give opinions on matters that are not within the expertise of lawyers (for example, financial statement analysis, economic forecasting and valuation). When an opinion depends on a matter not within the expertise of lawyers, an opinion giver is entitled to rely on a certificate from an appropriate source or an express assumption with regard to the matter.

2. Facts and Assumptions

2.1 *Reliance on Factual Information and Use of Assumptions.* Because the lawyers preparing a closing opinion (the "opinion preparers") typically will not have personal knowledge of all of the facts they need to support the opinions being given, they ordinarily are entitled to base those opinions on factual information provided by others, including their client, and on factual assumptions.

2.2 *Reliance on Facts Provided by Third Parties.* Opinion givers are entitled to rely on factual information provided by others unless the opinion preparers know that information to be false or unreliable. Information may be unreliable, for example, if it is irregular on its face or has been provided by an inappropriate source.

2.3 *Scope of Inquiry.* Opinion preparers are not expected to conduct a factual inquiry of the other lawyers in their law firm or a review of the firm's records, except to the extent they recognize that a particular lawyer is reasonably likely to have or a particular record is reasonably likely to contain information not otherwise known to them that they need to give an opinion.

2.4 *Reliance on Representations That Are Legal Conclusions.* An opinion should not be based on a representation that is tantamount to the legal conclusion it expresses. An opinion may, however, be based on a legal conclusion in a certificate of an appropriate government official.

2.5 *Factual Assumptions.* Some factual assumptions on which opinions are based need to be stated expressly; others do not. Examples of factual assumptions that ordinarily do not need to be stated expressly are assumptions of general application that apply regardless of the type of transaction or the nature of the parties. These include, for example, assumptions that copies of documents are identical to the originals, signatures are genuine, and the parties other than the opinion giver's client or a non-client whose obligations are covered by the opinion have the power and have taken the necessary action to enter into the

transaction, and the agreements those parties have entered into with the opinion giver's client are enforceable against them.

3. Law

3.1 *Covered Law.* When a closing opinion states that an opinion covers the law of a specific jurisdiction or particular laws, the opinion covers no other law or laws.

3.2 *Applicable Law.* An opinion on the law of a jurisdiction covers only the law of that jurisdiction that lawyers practicing in the jurisdiction, exercising customary professional diligence in similar circumstances, would reasonably recognize as being applicable to the client or transaction that is the subject of the opinion. A closing opinion does not cover some laws (for example, securities, tax and insolvency laws) that are otherwise applicable to the matters it addresses. A closing opinion also does not cover municipal and other local law. An opinion may, however, cover law that would not otherwise be covered if the closing opinion so states or the opinion does so expressly.

4. Miscellaneous

4.1 *Date.* A closing opinion speaks as of its date. An opinion giver has no obligation to update a closing opinion for subsequent events or legal developments.

4.2 *Reliance.* A closing opinion may be relied on only by its addressee and any other person expressly authorized to rely.

Ethics Update: Including Opinion Practice and UPL

I. Boone v. Quicken Loans, Inc..

A. Introduction.

In *Boone v. Quicken Loans, Inc.*,[1] the South Carolina Supreme Court provided guidance as to what constitutes adequate South Carolina supervision and involvement in each phase of a residential mortgage loan closing. Prior to the *Quicken Loans* decisions is was not clear what action was necessary to meet the attorney supervision requirements. *Quicken Loans* clarified the requisite level of attorney involvement and effectively provides a safe harbor for the conduct of residential mortgage loan closings.

B. Nature of the Case.

The case was brought as a declaratory judgment action in the original jurisdiction of the Supreme Court. The respondents were Quicken Loans, Inc., a corporation engaged in the business of making residential mortgage loans on a nationwide basis, and Title Source, Inc., which provides settlement services and title insurance across the country. The Petitioners were homeowners who had refinanced their mortgages with Quicken Loans; these homeowners alleged that Quicken Loans and Title Source engaged in the unauthorized practice of law, and sought to recover fees paid to Quicken Loans and to have their mortgage liens declared void. The homeowners also sought class certification and class relief.

C. Issue.

At issue was whether Quicken loans and Title Source, Inc. were engaged in the unauthorized practice of law by virtue of their mortgage loan closing process.

D. Decision of the Special Referee.

The Supreme Court referred the matter to Circuit Judge Diane Goodstein, to act as Special Referee. Judge Goodstein recommended that the Supreme Court find that the closing process used by Quicken Loans and Title Source constituted the unauthorized practice of law.

E. Decision of the Supreme Court.

The Supreme Court rejected these recommendations, and held that there was no unauthorized practice of law in the process before the Court. According to the Court, there is no UPL where the following requirements are met:

- A licensed South Carolina attorney is involved in each critical stage of the transaction.

[1] 420 S.C. 452, 803 S.E.2d 707 (2017)

- The South Carolina attorney is independent, such that the attorney exercises the attorney's independent professional judgment at key points in the transaction.

- Note: the court made clear that attorneys are not required to personally conduct the "clerical tasks" comprising a part of the transaction closing.

- In reaching its decision, the Court made a determination that requiring further attorney involvement would not provide further protection to the public from the dangers of the unauthorized practice of law.

F. The Quicken Loan/Title Source Closing Process.

The loans at issue were refinances – the borrowers already owned the property, and were simply seeking more favorable loan terms. The actual process was as follows:

- The homeowner interested in refinancing would first execute a loan application – typically this was done online.

- Next, the homeowner would speak with a Quicken Loan representative by telephone, at which time the homeowner would be notified of its right to select legal counsel (arising under South Carolina Code § 37-10-102) and determine whether in fact the homeowner had a preference for counsel.

  - If the homeowner had no preference for a specific attorney to handle the refinance, Quicken Loans would hire Title source.

- Title Source would contact a non-attorney abstractor by email to conduct the title search and prepare the title abstract. Title Source would in that email identify the subject property, and the scope of the search — which typically extended back two years prior to the current owner's vesting deed.

- The abstractor would submit the title report directly to Title Source via the Internet. Title Source would then forward the title report to a South Carolina attorney who would review the abstract and supporting documents. The South Carolina attorney would then issue a title "certificate," certifying that he had reviewed the title documents and that the proposed borrower's held fee simple title.

- Upon receipt of this title certificate, Title Source would prepare and submit to Quicken Loans a title commitment.

- Title Source and Quicken Loans would then schedule a closing and prepare closing package, including a settlement statement, promissory note, mortgage, and closing instructions.

- The closing attorney would review the closing package, verify that the title work had been certified by a South Carolina lawyer, that the closing documents were accurate and comply with law, and make any necessary corrections to the closing documents.

- The closing attorney then met with the borrower or borrowers, explained the documents, answered questions, and supervised the execution of the documents.

- Once the documents were executed, the attorney sent the executed documents to Title Source, along with instructions as to recordation and disbursement.

- After disbursement, Title Source provided the closing attorney with the closing ledger, allowing the closing attorney to confirm that disbursement have been made in accordance with the settlement statement.

- After recordation, a certified copy of each recorded document was transmitted to the closing attorney for review.

G. The Required Level of Attorney Involvement

The five phases of a residential mortgage loan closing is identified by the Supreme Court, and the clarification of those requirements as set forth by the Supreme Court in *Quicken Loans*, is as follows:

Phase 1: The preparation of deeds, notes, and other instruments.

- It is not necessary that a South Carolina lawyer prepare the real estate documents; it is sufficient that a South Carolina lawyer independent from the lender or other lay person preparing the documents review and revise the documents as necessary.

    - This is consistent with prior law. The prior rule had been that although real estate documents could be prepared by the lender, review of those documents was required by an independent South Carolina licensed attorney, and in particular an attorney who is not an employee of the entity preparing the documents must review the documents and makes any corrections necessary to cause them to comply with South Carolina law.[2]

Phase 2: Examination of Title.

- It is not necessary for an attorney to order the title examination from the abstractor — the abstractor is allowed to perform a title examination directly for a

[2] *See* Doe Law Firm v. Richardson, 371 S. C. 14, 17, 636 S. E.2d 866, 868 (2006); Doe v. McMaster, 355 S.C. 306, 314, 585 S.E.2d 773, 777 (2003).

title company (in this case Title Source), provided that the title work is reviewed by a South Carolina attorney prior to closing.

- Where, however, there is not attorney supervision, ordering title work and preparing a commitment by a title company is the unauthorized practice of law under *Doe v. McMaster*.[3] In that case, the title company ordered the abstract and prepared the title commitment. An attorney subsequently, however, reviewed the title commitment and performed "any necessary curative work" regarding the title. The *Doe v. McMaster* Court nevertheless held that, despite this review and curative work, these actions by the title company constituted the unauthorized practice of law. Is *Quicken Loans* reconcilable with *Doe v. McMaster?*

- It is still clear that the preparation of a title abstract and reports on the status of title without attorney supervision, the abstractor is engaged in the unauthorized practice of law.[4]

- The Court holds that it does not matter whether the title certificates are drafted by a non-lawyer, as long as the title certificates are reviewed by a South Carolina licensed lawyer.

Phase 3: Conduct of the Closing

The established requirements for attorney supervision with respect to closings, namely, (i) review of all of the closing documents, including the settlement statement, and (ii) physical presence at the closing to answer questions and review and explain the documents, and (iii) physical presence at the closing to supervise the execution of the documents were part of Quicken Loan's procedures, and thus were not before the Court for review.[5]

Phase 4: Recordation

It is not necessary that the closing attorney actually record; it is sufficient if the closing attorney supervises recordation by providing instructions to the recording party. This is consistent with prior law, under which the required supervision is met even if the instructions for recording are given to the recording office by a nonlawyer, provided that those instructions are given under the supervision of a lawyer.[6]

- In *Quicken*, in addition to specific instructions as to the manner of recordation, the title company was required to provide the recording date and book and page

[3] 355 S.C. 306, 585 S.E.2d 773 (2003).
[4] Ex parte Watson, 356 S.C. 432, 435; 589 S.E.2d 760, 761 (2003).
[5] As to this general requirement of physical presence at the closing, see In re Lester, 353 S.C. 246, 578 S.E.2d 7 (2003)
[6] State v. Buyers Serv. Co., 292 S.C. 426, 434 , 357 S.E.2d 15, 19 (1987); Doe v. McMaster, 355 S.C. 306, 315-16, 585 S.E.2d 773, 778 (2003).

numbers of the recorded loan documents, which recorded loan documents were then reviewed by the closing attorney.

- To come within the safe harbor of *Quicken Loans*, in addition to providing recording instructions, the closing attorney should review certified copies of the recorded documents post closing.

Phase 5: Disbursement

It was clear under prior law that a South Carolina attorney had to "oversee" disbursement.[7] Supreme Court had originally, however, declined to state what steps were necessary to carry out that oversight.[8] Instructions by the South Carolina attorney to the disbursing party to disburse in accordance with the closing statement appeared to be sufficient to satisfy that duty.[9]

Later, in the case of *In re Breckinridge*[10], the court stated that an attorney's duty to supervise disbursement of loan proceeds in a residential real estate transaction required that the attorney ensure that (i) the attorney has control over disbursement of loan proceeds and (ii) the attorney receive detailed verification that the disbursement was correctly made. Further, the *Breckinridge* Court held that verification of disbursements required not just review of a disbursement ledger, but also review of information from the relevant banking institution. *In re Breckinridge* also made clear that disbursement need not be made through the attorney's trust account.

7. Questions unresolved by *Quicken Loans*

- To what extent do the *Buyer's Service* UPL requirements apply to commercial, non-consumer and nonresidential transactions?
  - The Court's discussion refers to what activities constitute the unauthorized practice of law "in the context of a residential real estate transaction." The Court in its discussion of Buyer's Service notes that that seminal case first identified the steps in "a residential real estate purchase transaction" that constitute the practice of law.

[7] Doe v. Richardson, 371 S.C. 14, 18, 636 S.E.2d 866, 868 (2006).
[8] Id.
[9] In Doe v. Richardson, the supervision of disbursement was a letter directing the lender to disbursement in accordance with the HUD statement. The Court did not give any indication in its decision that this arrangement was inadequate.
[10] 416 S.C. 466, 77 S.E.2d 466 (2016).

II. Current UPL -Related Practices in Commercial Transactions.

A. Problem Areas.

- The permissible role of title companies and title agencies in ordering a title abstract and preparing a title commitment – where is the line between *Quicken Loans* and *Doe v. McMaster*?

- The role of title companies in the preparation of the settlement statement, the disbursement of funds, and the recordation of documents.

- The permissible role of attorney's licensed in states other than South Carolina in the conduct of commercial real estate closings.

- The absence of a physical closing that can be attended by South Carolina counsel.

  – See Ethics Advisory Opinion 05-16, permitting mail away opinions provided that (1) the attorney is providing competent representation to the client; (2) all aspects of the closing remain under the supervision of an attorney; and (3) the attorney complies with the duty to communicate stated in Rule 1.4, so as to maintain the attorney-client relationship and be in a position to explain and answer any questions about the documents sent to the client for signature.

  – Compare *In re Lester*, requiring physical presence at the closing.[11]

B. The Effect of Quicken Loans.

- Quicken Loans makes clear that a South Carolina attorney is not required to physically conduct the clerical aspects of a real estate closing, and arguably gives further support to the use of title companies for physically handling many mechanical aspects of the closing.

- Quicken Loans makes clear that tasks that otherwise would constitute the unauthorized practice of law (such as a layperson ordering or conducting a title examination) are not the unauthorized practice of law if properly reviewed and certified by a South Carolina attorney.

C. Use of UPL Certificates.

- Many South Carolina attorneys in transactions where title companies will play a significant role in the closing, or where there are out-of-state counsel not licensed in South Carolina playing a significant role in closing, will use UPL Certificates

[11] 353 S.C. 246, 578 S.E.2d 7 (2003).

as a due diligence and documentation tool to establish that there has been no unauthorized practice of law.

- Attached as Exhibit A is a form certificate for use as local counsel.

- Attached as Exhibit B is a form certificate for use where the roles of title counsel and other local counsel are bifurcated.

- Attached as Exhibit C is a simplified form certificate.

D. Use of UPL Language in closing instructions letters:

> "H. Compliance with South Carolina Law.
>
> 1. Title Company represents that the title examination upon which the Title Commitment is based was conducted by a South Carolina licensed attorney, namely _____, Esq. of _____, and the real estate documents related to the Transaction were or will be reviewed and approved by _____, Esq. of _____ to insure that they have been properly executed, witnessed, and notarized and are in recordable form.
>
> 2. The undersigned [attorney name] certifies that:
>
> (a) That (s)he is an attorney licensed to practice law in the State of South Carolina.
>
> (b) The real estate documents related to the Transaction were or will be reviewed and approved by the undersigned, and that the undersigned had or will have the opportunity to make corrections necessary to insure their compliance with South Carolina law.
>
> (c) The closing of the Transaction was or will be supervised by the undersigned and will be conducted in accordance with the instructions provided by the undersigned in this Agreement.
>
> (e) The disbursement of funds in connection with the Transaction was or will be supervised by the undersigned and will be conducted in accordance with the instructions provided by the undersigned in this Agreement.
>
> (f) That after completion of disbursement of the Escrowed Funds, he will review checks, ledgers, financial institution information and/or other evidence sufficient to verify disbursement as instructed."

D. Use of UPL Language in Purchase and Sale Agreement:

Compliance with South Carolina law. The parties acknowledge that South Carolina law may require that certain portions of the transactions contemplated hereby be conducted by or under the supervision of a South Carolina licensed attorney, and agree to take such steps as are necessary to cause the transactions contemplated hereby to conducted in accordance with such South Carolina law.

III. UPL Opinion-Related Issues

A. Need for and acceptance of UPL assumptions in third-party opinions.

B. Governmental Entity UPL Certificates – See Exhibit D

Exhibit A

Sample Local Counsel Certificate

SOUTH CAROLINA ATTORNEY CERTIFICATE

DATE: _____ __, 20__

RE: $_____ Loan ("Loan") by _____ ("Mortgagee"), to _____, as borrower, being secured by real property and fixtures of [Borrower] ([in such capacity,] "Mortgagor"), located in _____ County, South Carolina (the "Loan Transaction")

This certificate is provided by the undersigned attorney licensed to practice law in the State of South Carolina for the purpose of confirming that the aspects of the Loan Transaction listed below with respect to the real estate collateral located in South Carolina did not involve the unauthorized practice of law in the State of South Carolina. This certificate may be relied upon by Mortgagee in connection with its making the Loan and by _____ in connection with its involvement in the Loan Transaction as Mortgagee's local counsel.

The undersigned attorney certifies as follows:

1. South Carolina Attorney. The undersigned, _____ ("SC Attorney"), is an attorney in good standing, duly licensed in the State of South Carolina, and qualified to supervise the real estate matters as they relate to the closing of the Loan Transaction as described herein, and such involvement in the Loan Transaction does not constitute the unauthorized practice of law under the law of the state as it currently exists. SC Attorney is familiar with the closing requirements of South Carolina law and is not aware of any unauthorized practice of law in connection with the Loan Transaction. SC Attorney is not an employee of the title insurance underwriting company.

2. Title Search. The title search and the preparation of title reports or other documents related to the title insurance to be issued in connection for the Loan Transaction were undertaken or directly supervised by SC Attorney in the location described herein.

3. Real Estate Documents. SC Attorney supervised the execution and delivery of the [Mortgage Loan Documents *{define}*] related to the Loan Transaction [and other real estate related documents]. The [Mortgage Loan Documents] related to the Loan Transaction [and other real estate related documents] were or will be reviewed by SC Attorney prior to recordation to confirm that they are properly completed, including attaching a proper legal description, executed, witnessed and notarized sufficient for recording.

4. Closing. The closing of the Loan Transaction was or will be conducted or supervised by SC Attorney as it relates to all South Carolina real property assets of Mortgagor by providing written and, if requested, verbal, direction to Mortgagor and supervision and review of the execution and delivery of the [Mortgage Loan Documents] [and other real estate documents] that are to be recorded in South Carolina and all other documents governed by South Carolina law.

5. Recording of Documents. The recording of the mortgage and any releases or other real estate and lien related documents relating to the real property located in _____ County, South Carolina in order to close the Loan Transaction was or will be handled by SC Attorney or under the direct supervision of the SC Attorney.

6. Disbursement of Funds. The funds, if any, applicable to the Loan Transaction were or will be disbursed by the undersigned or the disbursement process was or will be supervised by SC Attorney by review and approval of closing statements and escrow instructions or other documentation as deemed necessary by SC Attorney.

This certificate is given in an effort to confirm compliance by the undersigned with the South Carolina attorney supervision requirements established by the South Carolina Supreme Court to date but is not a guarantee.

The undersigned does hereby execute this South Carolina Attorney Certificate as of the date first above written.

SC ATTORNEY

_____
Name: _____
SC Bar Number: _____

Exhibit B

Sample Bifurcated Title Counsel and Local Counsel Certificate

NO REPRESENTATION, WARRANTY, OR GUARANTY OF ANY KIND SHOULD BE IMPLIED THAT THIS FORM WILL BE DEEMED BY ANY COURT OF COMPETENT JURISDICTION TO BE SUFFICIENT, MEET THE BURDEN OF PROOF REGARDING SUPERVISION OF A REAL ESTATE CLOSING, OR CONFIRM THAT A REAL ESTATE TRANSACTION WILL NOT INVOLVE THE UNAUTHORIZED PRACTICE OF LAW.

ACKNOWLEDGMENT OF SOUTH CAROLINA ATTORNEYS

DATE: _____, 20__

RE: Loan by _____ ("Mortgagee"), _____, as borrower ("Mortgagor"), being secured by real property and fixtures located in _____ County, South Carolina (the "Loan Transaction")

This certificate is provided by the undersigned attorneys licensed to practice law in the State of South Carolina for the purpose of confirming between them that the aspects of the Loan Transaction listed below with respect to the real estate collateral located in South Carolina did not involve the unauthorized practice of law based on the attorney supervision requirements as currently established by the South Carolina Supreme Court for real estate transactions which have been satisfied between the delineated roles assumed and defined below by the undersigned South Carolina licensed attorneys.

The undersigned attorneys acknowledge the following with respect to their respective roles:

1. South Carolina Attorneys.

(a) _____ ("SC Title Attorney") is an attorney in good standing, licensed in the State of South Carolina, and able to supervise the real estate matters as they relate to the closing of the Loan Transaction as described herein. SC Title Attorney is familiar with the closing requirements of South Carolina law and is not aware of any unauthorized practice of law in connection with the Loan Transaction. SC Title Attorney is not an employee of the title insurance underwriting company.

(b) _____ ("Borrower's SC Counsel") is an attorney in good standing, licensed in the State of South Carolina, and able to supervise the execution and delivery of the South Carolina loan documents as described herein. Borrower's SC Counsel is familiar with the closing requirements of South Carolina law and is not aware of any unauthorized practice of law in connection with the Loan Transaction.

2. Title Search. The title search and the preparation of title reports or other documents related to the title insurance to be issued in connection for the Loan Transaction were undertaken or directly supervised by SC Title Attorney in the location described herein.

3. Execution of Documents. Borrower's SC Attorney supervised the execution and delivery of the loan documents related to the Loan Transaction [and other real estate related documents].

{For a mail-away closing} [The parties acknowledge the loan documents were executed outside of the state of South Carolina in a "mail-away closing." Borrower's SC Counsel was not present at the out-of-state closing and did not physically witness the execution of the loan documents signed outside of the state of South Carolina. However, Borrower's SC Attorney supervised the execution and delivery of the loan documents related to the Loan Transaction, to the extent governed by South Carolina law, by providing instructions regarding execution of the mortgage loan documents, by reviewing scanned copies of such executed loan documents prior to delivery and by

being available to advise the parties with respect to matters of state law in connection with the execution and delivery of such loan documents to the extent governed by state law.]

4. Real Estate Documents for Recording. The mortgage loan documents related to the Loan Transaction and other real estate related documents that will be recorded in South Carolina were or will be reviewed by SC Title Attorney prior to recordation to confirm that they are properly completed (including a proper legal description), executed, witnessed and notarized sufficient for recording.

5. Closing. The closing of the Loan Transaction was or will be conducted or supervised by SC Title Attorney as it relates to all South Carolina real property assets of Mortgagor by providing written and, if requested, verbal, direction, supervision and review of the execution of the real estate loan documents that are to be recorded in South Carolina and all other documents governed by South Carolina law.

6. Recording of Documents. Recording of the mortgage, assignment of leases and any releases or other real estate and lien related documents relating to the real property located in _____ County, South Carolina in order to close the Loan Transaction was or will be handled by SC Title Attorney or under SC Title Attorney's direct supervision.

7. Disbursement of Funds. The funds, if any, applicable to the Loan Transaction were or will be disbursed by the undersigned or the disbursement process was or will be supervised by SC Title Attorney by review and approval of closing statements and escrow instructions, or other documentation as deemed necessary by SC Title Attorney, among other things.

This certificate may be relied upon by the undersigned attorneys, by Mortgagor, by Mortgagee in connection with its making the Loan [and by [Borrower's SC Attorney] in connection with its involvement in the Loan Transaction for the purposes of rendering a local counsel enforceability opinion].

This certificate is given in an effort to confirm compliance by the undersigned with the South Carolina attorney supervision requirements established by the South Carolina Supreme Court to date but is not a guarantee.

IN WITNESS WHEREOF, the undersigned have hereby executed this certificate as of the date first set forth above.

SC TITLE ATTORNEY

_____
Print Name: _____
SC Bar Number: _____
(with respect to items 1(a), 2, 4, 5, 6 and 7 above)

BORROWER'S SC ATTORNEY

_____
Print Name: _____
SC Bar Number: _____
(with respect to items 1(b) and 3 above)

CONSENT OF MORTGAGOR:

Mortgagor is advised pursuant to Rule 1.2(c) of the South Carolina Rules of Professional Conduct as to this limited scope of representation for each lawyer and the division of closing responsibilities between the South Carolina attorneys and gives its informed consent by signing below.

MORTGAGOR

By: _____
Its: _____

Exhibit C

Sample Simplified Certificate

SOUTH CAROLINA ATTORNEY CERTIFICATE

TO: _____Title Insurance Company ("Title Insurance Company")

RE: _____, a South Carolina limited liability company ("Seller") sale to _____, a Delaware limited partnership ("Buyer"), of real property in _____ County, South Carolina (the "Transaction")

DATE: January 5, 2018

This certificate is provided by the undersigned attorneys licensed to practice law in the State of South Carolina for purposes of confirming that the aspects of the Transaction listed below did not or will not involve the unauthorized practice of law. This certificate may be relied upon by the Title Insurance Company and all other parties involved in the Transaction. The undersigned certifies as follows:

1. Title Search. The title search and the preparation of title reports or other documents related to the title for the Transaction were undertaken or supervised by the undersigned or the undersigned will confirm his/her satisfaction that a licensed South Carolina attorney will undertake or supervise the foregoing.

2. Real Estate and Loan Documents. The real estate and/or loan documents related to the Transaction were or will be reviewed by the undersigned, who had or will have the opportunity to make corrections necessary to insure their compliance with applicable law.

3. Closing. The closing of the Transaction was or will be conducted or supervised by the undersigned.

4. Recording of Documents. Document recording to complete the Transaction was or will be completed or supervised by the undersigned.

5. Disbursement of Funds. The funds, if any, applicable to the Transaction were or will be disbursed by the undersigned or the disbursement process was or will be reviewed and approved by the undersigned.

_____

Printed Name: _____
SC Bar Number: _____
(As to Items: 1 and 4)

_____

Printed Name: _____
SC Bar Number: _____
(As to Items: 2)

_____

Printed Name: _____
SC Bar Number: _____
(As to Items: 3 and 5)

Exhibit D

MORTGAGOR(s)

Borrower:

***Loan Number:**

Property Description:

***Lender/ Investor Number(s):**

Date of Note and Mortgage:

I, _____, a South Carolina licensed attorney, South Carolina Bar Number _____ do hereby certify, warrant and affirm as follows:

The above referenced loan has been closed in full compliance with all current applicable statutory and case law for the State of South Carolina regarding the *Unauthorized Practice of Law* ("**UPL**") and specifically real estate mortgage loan closings in South Carolina. Furthermore, and to delineate the requirements set forth under *State v. Buyers Service Co., Inc.*, 292 S.C. 426, 357 S.E. 2d 15 (1987) and all subsequent related case law and in particular *BAC Home Loan Servicing, L.P. v. Kinder*, 398 S.C. 619, 731 S.E. 2d 547 (2012), I hereby confirm, represent and warrant to the Lender, Investor, title insurance company and any other related parties that the UPL requirements have been met and that listed legal services have been performed or supervised by me. It is understood that these requirements are not set forth by way of limitation, but rather to confirm as to them specifically, as well as to confirm, represent and warrant that the Lender, its assignees, any Investors or title insurance companies may rely on them as well as any other lending requirements to ensure that the Note, Mortgage, and any guaranty agreements associated therewith, along with all other loan documents, are fully enforceable and will not be prejudiced in any way by the failure to comply with South Carolina's statutory, judicial, and regulatory requirements. These requirements include but are not limited to all of the following actions or services:

1. All legal instruments relating to this real estate transaction have been prepared and/or reviewed by a South Carolina licensed attorney;

2. The title abstract or search, along with any title commitment, has been reviewed and supervised by a South Carolina licensed attorney;

3. The real estate closing itself has been conducted and supervised by a South Carolina licensed attorney, and a South Carolina licensed attorney has explained to the borrowers the terms and provisions of the Note and Mortgage and all other legal documents associated with this transaction; and

4. The recording of documents has been or will be supervised by a South Carolina licensed attorney.

I hereby certify, represent and warrant the foregoing compliances this ____ day of _____, 20___.

_____ SC Bar Number _____

I (we) as Mortgagors for this loan attest and verify to the Lender and/or Investor that the above listed loan closing services were performed by and/or supervised by the above named South Carolina licensed attorney:

Mortgagor (Signature/Printed Name) _____

Dated_____