Hypothetical for Fall 2016 WGLO Conference

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Michael is a partner with a small firm in New York. On May 1, Michael receives a referral from Brian, a lawyer at a large firm in Houston, who is a close friend. Brian tells Michael that his client, an oil refining company called TexOil, is entering into a long-term financing arrangement with a Dallas-based fund, Lone Star Capital. The financing will allow TexOil to expand its business to purchase retail gas stations in Texarkana. Brian's law firm is handling the legal work for TexOil in the transaction, and the parties have agreed that the transaction will be governed by Texas law; but some of the collateral is in the form of treasuries that are held in New York banks, so the investment fund has asked for an opinion from New York counsel that this aspect of the transaction will not violate New York law to the extent it is applicable, including any provisions relating to usury. This request comes late in the game: the transaction is scheduled to close on May 14. Brian apologizes for the short notice but he and the parties assume this will be a simple and uncontroversial opinion.

Michael accepts the engagement. His engagement letter with TexOil provides that his firm is engaged to research and, if appropriate, provide a third-party opinion to Lone Star Capital on whether the security arrangement in the proposed transaction would be permissible under New York law. Brian sends Michael the draft transaction documents, which he says are essentially final and have been heavily negotiated among the parties for months. Brian tells Michael that he is hopeful that the New York aspect of the transaction will not be a problem, because the parties' negotiations have been contentious and any significant changes at this stage could crater the deal. Brian confides to Michael that TexOil is frustrated with Brian because his firm belatedly identified a number of legal impediments to the transaction that had to be worked through.

Step One:
Michael reviews the documents. He quickly concludes that the security aspect of the transaction presents no problems under New York law, and he is comfortable giving the opinion that the client has requested. Michael notices, however, that the transaction is structured to allow Lone Star to require accelerated payment, or impose a hefty increase in the interest rate, upon the occurrence of any "event of default" by TexOil, with only a 15-day cure period; "event of default" is defined to include among other things the failure to produce timely pricing and tax information regarding the sales of petroleum from the properties to be acquired. Based on Michael's experience with another client in Texas, he knows that the Texas Corporation Commission has in the past year been experiencing unusual delays (up to 30 days) in setting prices, so that TexOil may be highly exposed to business risk if it agrees to this provision.

Michael calls William, the general counsel of Michael's firm, and explains the situation. Michael tells William he plans to give the opinion as requested. He has not been engaged to represent TexOil on anything other than the narrow New York law issue. He doesn't want to make trouble for Brian. He presumes TexOil understands the business risk, which is not a lawyer's job anyway. He is concerned that if he raises an issue about the default provision he will cause a problem with the deal. How should William respond?

Step Two:
William remarks to Michael that another partner of their New York firm, Keith, represents Ark-Petro, an Arkansas-based oil company that does substantial business in Texas. Keith has represented Ark-Petro for many years. Michael calls Keith and asks whether Ark-Petro has a presence in Texarkana. Keith says that Ark-Petro has long been the largest owner of retail gas stations in the Texarkana metropolitan area. Coincidentally, Keith says, he recently got a call from the general counsel of Ark-Petro (whose name, of course, is Charlie), asking him to look into the antitrust implications of a potential expansion of that business and corresponding pricing strategy, which Keith has begun to do. Charlie is excited about this business plan, which he thinks could drive down petroleum prices so that it would be difficult for anyone to compete. Michael remarks to his partner, Keith, that Ark-Petro's plan would severely impact the value of the gas station purchases TexOil is planning to make, damaging TexOil and jeopardizing the collateral of its lender Lone Star.

Michael and Keith decide they had better talk to William. How should William respond? Can the firm represent both TexOil in giving the opinion and Ark-Petro in giving the antitrust advice? If not, can it represent either TexOil or Ark-Petro? Is the firm required, or even permitted to withdraw from either engagement? If the firm needs to withdraw from either or both representations, can it explain the reasons to the clients?