Private lawsuits, public lawyers

Should you have a binding arbitration clause in your attorney fee agreement?

By Karen Stromeyer and Timothy Halloran

Should you or shouldn't you? When faced with a legal malpractice lawsuit from a former client, many lawyers have regrets about whether they should, or should not have included a binding arbitration agreement in their fee contract. Here is the answer: There really is no right answer. There are distinct advantages and disadvantages to being in arbitration and being in civil court. The decision depends on your preferences and how you balance each pro and con. What follows are a few things to consider before making your decision, and tips for drafting an arbitration clause if you decide to include it.

A well-drafted arbitration clause will be enforced

California law expresses a clear public policy in favor of the enforceability of arbitration provisions within contracts as a speedy and relatively inexpensive means of dispute resolution. (*Moncharsh v. Heily & Blase* (1992) 3 Cal.4th 1, 9.) To that end, Code of Civil procedure section 1281 states: "A written agreement to submit to arbitration an existing controversy or a controversy thereafter arising is valid, enforceable and irrevocable, save upon such grounds as exist for the revocation of any contract." (Code Civ. Proc., § 1281.) Courts will indulge every intendment to give effect to arbitration clauses. (*Moncharsh v. Heily & Blase*, *supra*, 3 Cal.4th at 9.) An attorney may ethically, and without conflict of interest, include in an initial retainer agreement with a client a provision requiring the arbitration of both fee disputes and future legal malpractice claims. (*Powers v. Dickson, Carlson & Campillo* (1997) 54 Cal.App.4th 1102, 1108-1109; Cal. State Bar Form. Opn. 1989-116.)[1]

Specific issues with agreements to arbitrate fee disputes

Even in a good attorney-client relationship, fee disputes can arise. When they do, lawyers should be aware that arbitration of disputes relating to attorney's fees and costs are governed by Business and Professions Code section 6200. That section governs any attorney-client fee disputes and voids any contractual arbitration provisions that are in conflict with it. (*Alternative Systems Inc. v. Carey* (1998) 67 Cal.App.4th 1034, 1044; California State Bar Formal Op. 1981-56.)

Business and Professions Code section 6200 et. seq., also known as the Mandatory Fee Arbitration Act, also requires that before any lawsuit or other proceeding can go forward, the lawyer must comply with the non-binding Mandatory Fee Arbitration ("MFA") notice requirement. Prior to or at the time of service of summons of your fee action, the lawyer must give the client a preliminary notice of the right to participate in nonbinding fee arbitration. (Bus. & Prof. Code, § 6201(a).) If the attorney fails to provide the required notice, the client may stay the action or other proceeding by filing a request for MFA. If the attorney has sued the client, the client may submit a request to participate in MFA prior to answering the complaint. MFA is completely voluntary for the client, but if the client commences non-binding MFA, it is mandatory for the attorney to participate. (Bus. & Prof. Code, § 6200 (c).)

Generally, because the MFA is non-binding, either party may seek trial de novo of their claims. (Bus. & Prof. Code § 6204(a).)

However, if a client waives non-binding MFA, by failing to formally elect it or filing an affirmative civil action, or following the completion of an MFA, then any pre-dispute arbitration agreement between the client and the attorney will be enforced as to all disputes, including fees. (*Schatz v. Allen Matkins Leck Gamble & Mallory LLP* (2009) 45 Cal.4th 557, 574.) Therefore, while no arbitration provision will relieve you of mandatory participation in MFA, once it is done, any binding contractual arbitration provision can be fully enforced, and the client does not have a right to trial de novo in court.

Advantages of arbitration over civil litigation

Many attorneys feel that there are significant advantages to including a binding arbitration provision in their legal services contract. These include:

- Privacy. Many attorneys highly value that their name or law firm is not being called in open court or being on the docket as a legal malpractice defendant. This can be incredibly awkward or potentially embarrassing if you are appearing in the same court as an advocate, and arbitrations have a much greater level of privacy of deposition and other transcripts and pleadings.
- Avoids risks of a jury that may be sympathetic to an unsophisticated client.
- Can be less expensive in that discovery is typically limited.
- Can be faster than trial, especially in light of the recent budgetary issues faced by the courts.

• Arbitrators are often more experienced and comfortable with complicated (and typically dry) issues of duty, breach, and causation, as well as the case-within-a-case format present in these cases.

Disadvantages

On balance, there are many practical disadvantages to arbitration, particularly for your defense counsel:

• Some lawyers can find it uncomfortable to arbitrate malpractice claims in front of arbitrators (who usually also serve as mediators) that they use regularly.

• Cases against attorneys are often disposed of by demurrer, anti-SLAPP, summary judgment, or other dispositive motion. Even if permitted, these motions are rarely successful in arbitration, where strict rules of pleading and evidence are relaxed, increasing the likelihood that the matter will require a full-blown arbitration proceeding to resolve.

• Can be more costly for all parties because arbitrators charge in the neighborhood of $5,000 per day, for each day of the arbitration hearing. While this is much more expensive than a court hearing, arbitration is unique in that this cost is split with the plaintiff. Therefore, unlike a typical civil case, the plaintiff is facing large costs that are not recoverable unless there is a contractual provision in your fee agreement awarding prevailing party fees and costs. This can in many cases serve as an early deterrent to a plaintiff when it is a lower exposure case.

• Absent agreement otherwise, discovery is limited, the Civil Discovery Act of the Code of Civil Procedure, does not apply. The American Arbitration Association ("AAA"), and Judicial Arbitration and Mediation Service ("JAMS") each have their own rules and procedures, and anything else has to be agreed upon by the parties, usually at the initial conference with the arbitrator.

• Relaxed rules of evidence and procedure mean most anything can be introduced to be considered by the arbitrator, and left to the arbitrator's discretion as to how much weight it is to be given.

• Lack of subpoena power can drastically reduce the ability to procure third-party testimony.

• The arbitrator is not bound by California law. (See *Moncharsh v. Heily & Blase*, *supra*, 3 Cal.4th at 10-11.) "Arbitrators, unless specifically required to act in conformity with rules of law, may base their decision upon broad principles of justice and equity, and in doing so may expressly or impliedly reject a claim that a party might successfully have asserted in a judicial action." (*Sapp v. Barenfeld* (1949) 34 Cal.2d 515, 523.)

• The general rule that, with narrow exceptions, an arbitrator's decision cannot be reviewed for errors of fact or law. (See *Moncharsh v. Heily & Blase*, *supra*, 3 Cal.4th at 10-11.) An award reached by an arbitrator pursuant to a contractual agreement to arbitrate is not subject to judicial review except on the grounds set forth in sections 1286.2[2] (to vacate) and 1286.6[3] (for correction). The existence of an error of law apparent on the face of the award that causes substantial injustice does not provide grounds for judicial review. Also, it is well settled that arbitrators do not exceed their powers merely because they assign an erroneous reason for their decision. (*O'Malley v. Petroleum Maintenance Co.* (1957) 48 Cal.2d 107, 110, 111.)

• No right to appeal an arbitration award means the loss of leverage to resolve a matter for less than the award.

• Even if the action goes through arbitration, the award must be confirmed via a petition that is filed in court to create an enforceable judgment. (Code Civ. Proc. § 1285). This process deprives the parties of privacy and confidentiality.

How to do it

If, on balance for you and/or your firm, the advantages of arbitration outweigh, here are some things to consider in drafting the provision in your contract:

• Make the arbitration clause "conspicuous, plain, and clear.[4]" Either set it apart within the engagement letter or fee contract (through capital letters, bold type, etc.), or set it apart in a separate agreement, which is also signed by the client. Ensure that the client understands the clause covers malpractice claims.

• Obviously it should include the word "malpractice," and state in simple language that by signing the agreement that the client is agreeing to arbitrate any claims regarding the professional services rendered.

• Have language recommending that the client obtain outside legal advice before agreeing to the clause.

• Ensure the effects of the clause are fully disclosed to the client. For example, the client should understand that they are waiving trial by jury, broad discovery, and the right to appeal.

• Consider any specific conditions you want to include, for example:

• Which ADR provider would you prefer: JAMS? AAA?

• How many arbitrators shall comprise the panel?

• Any specific qualifications for the arbitrator, such as ex-judge?

• Where should the venue be?

• What type of discovery should be allowed?

• What procedural rules should apply?

• Should the arbitration be conducted pursuant to the laws of the State of California?

Example: Arbitration clause

> Client and attorney agree that any dispute arising out of this agreement or attorney representation will be resolved exclusively by submission to binding arbitration under the rules of the American Arbitration Association. This includes, but is not limited to, any claim or dispute regarding billing/fees or attorney's performance of services including for malpractice, negligence, breach of fiduciary duty, breach of contract, or the like that you may later wish to assert against us.

Arbitration shall be before a single neutral arbitrator, selected pursuant to the rules of the American Arbitration Association, and determined by arbitration in San Francisco County. Attorney and Client shall each have the right to discovery in connection with any arbitration proceeding in accordance with Code of Civil Procedure section 1283.05. In agreeing to this arbitration provision, Attorney and Client are specifically giving up any right they may possess to have such disputes decided in court or in a trial by jury, and all judicial rights including the right to appeal from the decision of the arbitrator.

By signing this agreement, Client acknowledges that Client has read and understands this provision. Client acknowledges that Client has time to consider this provision and has been advised of the right to consult with independent counsel prior to accepting this agreement for binding arbitration.

Conclusion

Getting sued by your client is never good news. If you are in binding arbitration or in court the personal costs to you and your practice will be significant. On balance, if your practice is one that handles mostly lower exposure cases, you may benefit from the deterrent effect of the higher costs of an arbitration proceeding and include a binding arbitration clause in your fee agreements. On the other hand, if your practice involves mostly larger exposure cases it is likely more beneficial to remain in court where your chances of an early dismissal on pleading issues or via motion practice are greater, although public exposure is also greater. As defense attorneys who defend attorneys, we believe in the jury system and think that the jury usually gets it right.


Stromeyer

Karen Stromeyer is a senior associate attorney at Murphy, Pearson, Bradley & Feeney *with a practice emphasizing general civil litigation including defending lawyers against claims of professional liability. Prior to joining Murphy, Pearson, Bradley & Feeney, she spent several years as an associate at a prominent Plaintiff's firm in San Francisco where she represented catastrophically injured individuals.*


Halloran

Timothy Halloran is a senior partner at Murphy, Pearson, Bradley & Feeney. *An experienced trial lawyer and civil litigator, he has tried over 20 legal malpractice cases to jury verdict and is a member of the American Board of Trial Advocates, is a Certified Legal Malpractice Specialist, and currently sits on the State Bar Legal Malpractice Law Advisory Committee.*

Endnotes

[1] If you are going to include it in your agreement, make sure you check with your Errors & Omissions insurance carrier, this may reduce your premium cost.

[2] Code of Civil Procedure section 1286.2 states: "(a) Subject to Section 1286.4, the court shall vacate the award if the court determines any of the following: (1) The award was procured by corruption, fraud or other undue means. (2) There was corruption in any of the arbitrators. (3) The rights of the party were substantially prejudiced by misconduct of a neutral arbitrator. (4) The arbitrators exceeded their powers and the award cannot be corrected without affecting the merits of the decision upon the controversy submitted. (5) The rights of the party were substantially prejudiced by the refusal of the arbitrators to postpone the hearing upon sufficient cause being shown therefore or by the refusal of the arbitrators to hear evidence material to the controversy or by other conduct of the arbitrators contrary to the provisions of this title. (6) An arbitrator making the award either: (A) failed to disclose within the time required for disclosure a ground for disqualification of which the arbitrator was then aware; or (B) was subject to disqualification upon grounds specified in Section 1281.91 but failed upon receipt of timely demand to disqualify himself or herself as required by that provision. However, this subdivision does not apply to arbitration proceedings conducted under a collective bargaining agreement between employers and employees or between their respective representatives."

[3] Code of Civil Procedure section 1286.6 states: "Subject to Section 1286.8, the court, unless it vacates the award pursuant to Section 1286.2, shall correct the award and confirm it as corrected if the court determines that: (a) There was an evident miscalculation of figures or an evident mistake in the description of any person, thing or property referred to in the award; (b) The arbitrators exceeded their powers but the award may be corrected without affecting the merits of the decision upon the controversy submitted; or (c) The award is imperfect in a matter of form, not affecting the merits of the controversy."

[4] See Cal. State Bar Form. Opn. 1989–116, fn. 5.