Mandatory Fee Arbitration Survives Schatz’ Shots

By Michael J. Fish and Jill Sperber

The recent decision by the California Supreme Court in Schatz v. Allen Matkins, 45 Cal. 4th 557 (2009), resolves the previously vexing issue of whether an agreement to arbitrate set forth in a retainer agreement made before any dispute arises may be enforced to substitute for a trial de novo following non-binding mandatory fee arbitration (“MFA”) required by the Business & Professions Code. The Schatz Court concluded that the MFA statutory scheme providing for a trial in court following

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non-binding arbitration does not stand as an obstacle to enforcement of a preexisting agreement to binding arbitration, following non-binding MFA.

So, what does this really mean for attorneys with arbitration clauses in their retainer agreements that call for private arbitration to resolve attorney fee disputes?

Under the Mandatory Fee Arbitration Act (MFAA), Article 13 of the California State Bar Act, Bus. & Prof.Code, § 6200 et seq., when there is a fee dispute between an attorney and a client, the client may choose to submit the matter to mandatory fee arbitration (MFA) by a local bar association. If the client elects such arbitration, the attorney must agree to arbitrate in the MFA forum (hence “mandatory” fee arbitration.) The award in the arbitration will be binding, however, only if the attorney and client so agree in writing after the dispute has arisen [Bus. & Prof. Code § 6204(a)]. Otherwise, the decision in the mandatory fee arbitration is non-binding, meaning that either party may request a trial de novo in court within 30 days after the arbitration award is served. Although the Business and Professions Code sets forth the right to request a trial de novo to challenge the award in the MFA by filing an action in the court having jurisdiction over the amount in controversy, it is silent with respect to the right to compel private arbitration after non-binding MFA instead of the trial de novo in court.

In recent years, an increasing number of attorney-client retainer agreements contain language providing that disputes between the attorney and the client shall be submitted to binding arbitration. Obviously such agreements, entered into at the commencement of the attorney-client relationship, precede the occurrence of any dispute as to fees and costs and do not deprive the client of the right to participate in the MFA process. Some arbitration clauses specifically reference disputes regarding fees or costs, while others attempt to deal globally with all attorney-client disagreements. So the question arises in some cases as to the effect of pre-existing

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fee arbitration agreements on the Mandatory Fee Arbitration ("MFA") pro-

gram. In particular, may a pre-existing arbitration agreement between the attorney and client be enforced, thereby depriving a party of his or her statutory right to request a trial in court as provided for in the MFA statutes following non-binding MFA?
The Proliferation of Private Fee Arbitration Agreements

The question of whether the parties' agreement to arbitrate fee and/or cost disputes is enforceable or is superseded by the MFAA is significant in light of the proliferation of arbitration clauses in attorney retainer agreements during the last two decades. This proliferation is understandable, and correlates with the recent and rapid expansion of arbitration as a dispute resolution mechanism.

It appears well established that lawyers and clients are free to enter into agreements for binding arbitration of future disputes with the sole exception of potential disputes regarding fees or costs governed by the MFA system and Business & Professions Code § 6204 in particular. Agreements to arbitrate legal malpractice cases have specifically been found to be valid. See Powers v. Dickson, Carlson & Campillo, 54 Cal. App. 4th 1102, 1115 (1997). If there is an agreement between the lawyer and the client specifying that both will participate in the MFA program in the event of a dispute as to fees and costs, that agreement is enforceable under MFA. An MFA arbitration clause should be considered for inclusion in a retainer agreement because it enables the attorney, not just the client, to require that fee disputes be resolved through MFA. In those cases, the attorney may request MFA and MFA will then be mandatory for the client. But no agreement that the MFA award as to fees or costs will be binding is valid unless that specific agreement is entered into after the dispute has arisen [Bus. & Prof. Code § 6204(a)].

Notwithstanding these more specific arbitration provisions, attorney-client fee agreements frequently call generally for binding arbitration of all disputes without reference to MFA or without separate or specific consideration or mention of disputes regarding fees and costs. The MFA statute gives the client the absolute right to insist upon arbitration — either advisory or, if all parties

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agree, binding — under Business & Pro-fessions Code §§ 6200 et seq. The challenge, however, is how to apply arbitration agreements which either (a) fail to separate out disputes over fees and costs or (b) provide

The Schatz v. Allen Matkins Opinion

In Schatz, the Supreme Court decided the issue of whether a court may compel binding contractual arbitration in lieu of a trial de novo in court requested by the client following non-binding MFA where there is a preexisting arbitration agreement. The Court concluded that the MFA statutory scheme providing the right to a trial de novo after non-binding MFA does not stand as an obstacle to enforcement of a valid preexisting binding fee arbitration agreement, thereby then directing the matter to contractual arbitration rather than trial. Schatz, supra, 45 Cal. 4th at 575.

The client in Schatz had accepted a binding arbitration clause in the fee agreement. The parties proceeded to non-binding MFA through a local bar association program. Dissatisfied with the non-binding MFA award, the client filed a judicial action for a trial de novo. The respondent attorneys petitioned the court to compel binding arbitration instead, pursuant to their preexisting binding arbitration agreement with the client. The trial court agreed with the client, who had argued that a private arbitration agreement cannot trump his statutory right to a trial de novo following non-binding MFA. The attorneys had argued that binding contractual arbitration would satisfy the MFA statutes’ de novo trial requirement. On appeal, the court of appeal agreed with the trial court, resulting in the attorneys’ petition in the Supreme Court seeking review.

The Supreme Court analyzed the interplay and, resolved any ambiguity, within the MFA statutes between the provision allowing for an automatic stay of any pending litigation “or other proceedings” (Bus. & Prof. Code § 6201) and the right of the parties to finalize

Several unresolved practice issues exist in the wake of the Schatz case. For example, the MFA statute addresses only how to reject a non-binding MFA award by filing an action in court.that the client’s rights to MFA arbitration of fees and costs are preserved but — if non-binding MFA arbitration is elected — any subsequent resolution must be through binding arbitration rather than through trial de novo in a court.
their dispute with binding MFA (after the fee dispute has arisen) [Bus. & Prof. Code § 6204(a)]. The Court concluded that the statute conferring the right to make MFA binding does not govern how the parties may resolve the case after non-binding MFA. In other words, an agreement for binding arbitration following an unsatisfactory non-binding MFA award is not prohibited by the MFA statutory scheme and satisfies the requirement of a trial de novo. The Court concluded that “the MFAA [Mandatory Fee Arbitration Act] does not stand as an obstacle to the enforcement of a valid agreement to arbitrate pursuant to the CAA [California Arbitration Act].” Schatz, supra, 45 Cal. 4th at 575.

— Parting Practice Tips —
What impact, if any, does the Schatz opinion have on Mandatory Fee Arbitration?

— In Brief —

• The client’s right to MFA remains intact notwithstanding a preexisting arbitration agreement. The client continues to have the right to request MFA, notwithstanding a preexisting arbitration agreement to resolve fee disputes through binding arbitration. The Schatz case does not take away the rights of the client to receive the required Notice of Right to Arbitration form, request MFA with or without Notice from the attorney, or participate in MFA.

• A preexisting binding fee arbitration agreement still does not control the nature of any MFA requested. The client and attorney may still choose either binding or non-binding MFA after the fee dispute has arisen. The Schatz case does not require that the MFA be binding even if the preexisting arbitration agreement requires binding fee arbitration. Nor does Schatz preclude the client and attorney from agreeing that the MFA will be binding after the fee dispute has arisen.

• Following non-binding MFA, a party’s statutory right to a trial de novo may be satisfied by another arbitration pursuant to the parties’ preexisting contract to arbitrate. If the parties previously agreed to arbitrate their fee disputes, then the court may
compel arbitration in lieu of a trial *de novo* in civil court. In other words, arbitration may substitute for a trial *de novo* after non-binding MFA according to a prior arbitration agreement without offending the MFA statutes.

- **A non-binding MFA award may still become binding by operation of law after the passage of 30 days notwithstanding an otherwise enforceable preexisting contractual arbitration agreement.** The *Schatz* case does not affect the time period or ability of a party to challenge a non-binding MFA award. It only potentially affects the forum where the fee dispute will be re-heard, if requested within the required time period.

--- **Some Unknowns** ---

Several unresolved practice issues exist in the wake of the *Schatz* case. For example, the MFA statute addresses only how to reject a non-binding MFA award by filing an action in court. It remains to be seen whether filing a request directly with the parties' chosen arbitration provider within the required time period, without filing an “action” in court, will also operate to effectively reject an award. In addition, while the MFA statutes expressly provide for attorney’s fees and costs to the prevailing party in a subsequent trial following MFA, it can only be assumed that the same provision would apply for the prevailing party in a subsequent arbitration.

Another big issue up for grabs is whether a pre-dispute agreement purporting to waive the client’s right to MFA under the Business & Professions Code and to submit all disputes to private arbitration is enforceable. The MFA statutory scheme expressly provides the manner in which the client can waive MFA, none of which includes a pre-dispute MFA waiver agreement between the parties. [See Bus. & Prof. Code § 6201(a), (d).] The reported cases discussing MFA have not addressed this precise issue. But they imply that such a clause would not be upheld given the unique consumer protection underpinnings of the MFA Act. Indeed, the *Schatz* court cited its earlier discussion of the statute’s history in *Aguilar v. Lerner*, 32 Cal. 4th 974, 983 (2004) and concurred with the Court of Appeal that the legislative history of the MFAA shows “it was intended to be a consumer oriented piece of legislation designed to address disparities in bargaining power between attorneys and clients.” *Schatz, supra*, 45 Cal. 4th at 575, footnote 3. In contrast to private arbitration, the benefits of MFA include accessibility to clients representing themselves, fewer formalities, and generally, lower costs, offering distinct consumer protection advantages.

But the Court’s holding in *Schatz* enforcing private arbitration in lieu of a trial in court after non-binding MFA admittedly jeopardizes any assumption that a client’s pre-dispute waiver of MFA would be found unenforceable. Arguably, because MFA may proceed as non-binding, the usual goals of alternative dispute resolution, *i.e.*, expedi- ence and finality, may not always be achieved.

It may be prudent, for numerous reasons, for attorneys to include arbitration clauses in retainer agreements. In doing so, however, attorneys must understand the limitations and obligations imposed by the Mandatory Fee Arbitration Act and its impact on any such provisions in the retainer agreement. Even in the wake of *Schatz*, the client’s right to invoke mandatory fee arbitration under the MFA Act — whether the award is non-binding, binding (because the parties agree to make it such after the dispute arises), or becomes binding by operation of law — is alive and well.