Digest: Schatz v. Allen Matkins Leck Gamble and Mallory LLP

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Opinion by Moreno, J., expressing the unanimous view of the court.

Issue

Does the Mandatory Fee Arbitration Act ("MFAA")[1] preclude the enforcement of a valid agreement to arbitrate under the California Arbitration Act ("CAA")[2]?

Facts

In February 1999, Dr. Richard A. Schatz ("Schatz") retained the law firm of Allen Matkins Leck Gamble & Mallory LLP ("Allen Matkins") to represent him in a lawsuit regarding the assignment of income from a partnership.[3] The retainer agreement contained a provision stating that the agreement applied to "any additional matters we handle on your behalf or at your direction."[4] The arbitration provision of the agreement provided that Schatz could "line out" the arbitration section if he did not agree to it. However, Schatz did not line out the arbitration provision and thus agreed that "in the event of any dispute arising out of or relating to this agreement, our relationship, or the services performed (including but not limited to disputes regarding attorney's fees or costs . . .), such dispute shall be resolved by submission to binding arbitration . . . ."[5]

In February 2000, Allen Matkins represented Schatz in an easement dispute; no new retainer agreement was signed at that time.[6] Schatz paid Allen Matkins $179,088.69 for their work in the easement case, but when he ceased payments shortly before the case went to trial, Allen Matkins demanded an additional

1 CAL. BUS. & PROF. CODE, §§ 6200–6206 (West 2009).
2 CAL. CIV. PRO. CODE §§ 1280–1294.2 (West 2008).
3 *Schatz v. Allen Matkins Leck Gamble and Mallory LLP*, 198 P.3d 1109, 1112 (Cal. 2009).
4 *Id.*
5 *Id.*
6 *Id.*

$169,917.42 in a letter dated April 2003.[7] Schatz failed to respond to the letter, and in January of 2004 Allen Matkins invoked the arbitration provision of the original retainer agreement.[8] Schatz alleged that the arbitration provision did not apply because the retainer did not mention the easement litigation and the reference to "additional matters" was not sufficiently emphasized.[9] Schatz also claimed that the arbitration provision was unenforceable under *Alternative Systems v. Carey* and that he was entitled to invoke MFAA and exercise his "statutory rights to nonbinding fee arbitration, and if he so elects, trial *de novo* before a jury."[10]

Allen Maktins disagreed with Schatz's assessment of the arbitration provision but agreed to nonbinding arbitration under the MFAA.[11] When the arbitrator ruled in favor of Allen Matkins, Schatz filed a complaint for "trial *de novo*, declaratory relief, and refund of attorney fees."[12] In reply, Allen Matkins filed a petition to compel binding arbitration under the original retainer agreement.[13] Schatz opposed, arguing that *Alternative Systems'* construction of the MFAA nullified the binding arbitration provision.[14] Allen Matkins replied, asserting binding contractual arbitration would fulfill the MFAA's *de novo* trial requirement because the California Supreme Court impliedly rejected the holding in *Advantage Systems*.[15]

The trial court found for Schatz and the court of appeal affirmed.[16] The California Supreme Court granted Allen Matkin's petition for review.[17]

Analysis

The court began with a comparison of the MFAA and the CAA, recognizing them as "separate and distinct" schemes.[18] While the CAA applies to almost any civil dispute, the MFAA only covers disputes regarding legal fees and costs.[19] Additionally, the obligations to arbitrate under the MFAA are

7 *Id.*
8 *Id.* at 1112.
9 *Id.* at 1112–13.
10 *Id.* (citing Alternative Systems v. Carey, 67 Cal.App.4th 1034 (1998)) (italics added).
11 *Id.*
12 *Id.* (italics added).
13 *Id.*
14 *Id.*
15 *Id.*
16 *Id.*
17 *Id.*
18 *Id.*
19 *Id.* at 1114.

statutory, thus, even in the absence of an agreement to arbitrate, a client may call for arbitration under the MFAA while under standard arbitration, both parties must agree to arbitrate.[20] Under the MFAA, an attorney cannot compel a client to arbitrate an agreement, but a client may compel an attorney to do so.[21] Arbitration awards granted under the MFAA are not binding and either party may seek trial *de novo* or the parties may agree that the arbitration is binding.[22] The MFAA does not expressly reference the CAA, but it provides that an attorney must give written notice to a client "prior to or at the commencement of any other proceeding against the client under a contract between attorney and client which provides for an alternative to arbitration . . . for recovery of fees, costs, or both."[23] In *Aguilar v. Lerner*, the California Supreme Court inferred the clause "any other proceeding against the client under a contract between attorney and client" to include contractual arbitration under CAA.[24] The MFAA states that if an attorney engages in any other proceedings and the client is entitled to arbitration under the MFAA, then the client may request a stay of the other proceeding.[25] The MFAA also provides that parties may consent in writing to be bound by an arbitrator's award at any time, but that in the absence of a written agreement to bind, both parties are entitled to a trial after arbitration is timely sought.[26]

The court then delved into the decisions in *Alternative Systems* and *Aguilar*, explaining that they were "critical to understanding" the present case.[27] In *Alternative Systems*, the client and lawyer had an arbitration agreement but the client invoked arbitration under the MFAA.[28] After the MFAA arbitration, the client rejected the award and filed for trial *de novo*.[29] Subsequently, the dispute was litigated by the American Arbitration Association over the objections of the client who challenged the arbitrator's jurisdiction; the arbitrator found for the attorney and the client filed a motion to vacate the arbitrator's award because "contractual arbitration was

20 *Id.*
21 *Id.*
22 *Id.*
23 *Id.* (emphasis omitted).
24 *Id.* (citing Aguilar v. Lerner, 88 P.3d 24 (Cal. 2004)).
25 *Id.*
26 *Id.* at 1115.
27 *Id.*
28 *Id.* (citing Alternative Systems v. Carey, 67 Cal.App.4th 1034 (1998)).
29 *Id.*

'preempted by the MFAA with its right to trial *de novo*."[30] The trial court denied the motion but the court of appeal reversed.[31]

The court of appeal in *Alternative Systems* emphasized that the 1996 amendments to the MFAA strengthened client protections so that stays applied to *any* proceedings initiated by an attorney to resolve a fee dispute.[32] The court pointed out that the public policy behind the MFAA was to reduce disparity in bargaining power in attorney fee matters by providing the client the opportunity to elect arbitration of a fee dispute, unless that client has already agreed in writing to arbitrate all fee disputes.[33] The court also noted that the MFAA requires a written waiver of the right to trial *de novo* after the dispute arises. Additionally, the court rejected the attorney's contention that the American Arbitration Association ("AAA") arbitration would act as "trial after arbitration" under the MFAA.[34]

In *Aguilar*, the client sued the attorney waiving his right to MFAA arbitration.[35] The attorney filed a motion to compel binding arbitration under CAA.[36] The client opposed, claiming that under MFAA a client could not be compelled to arbitrate because arbitration was optional.[37] The court found that the client had waived his rights to the MFAA arbitration and thus, waived any rights afforded him under the MFAA scheme.[38] The court refused to determine whether the client was able to overcome the motion to compel had he not waived his MFAA rights.[39] However, in a concurring opinion Justice Chin expressly addressed that issue.[40]

First, Justice Chin reiterated the MFAA mandate that an attorney must inform the client of his or her rights under the MFAA before or contemporaneous to commencing "an action [or] . . . *any other proceeding* against the client under a contract between attorney and client which provides for an alternative to arbitration . . . ."[41] He emphasized that the "italicized language" indicated parties may contract to use an alternative proceeding

30 *Id.* (italics added).
31 *Id.*
32 *Id.*
33 *Id.*
34 *Id.* at 1116.
35 *Id.* (citing Aguilar v. Lerner, 88 P.3d 24 (Cal. 2004)).
36 *Id.*
37 *Id.*
38 *Id.*
39 *Id.*
40 *Id.* (citing *Aguilar*, 88 P.3d 24 (Cal. 2004) (Chin, J., concurring)).
41 *Id.* (emphasis in original).

to resolve their dispute rather than resorting to judicial action.[42] Justice Chin went on to state that if a client invoked MFAA, the Act would provide a stay of other proceedings until the MFAA arbitration was completed; but only until the MFAA arbitration was completed.[43] While Justice Chin acknowledged that the statutory language of the MFAA lacked clarity, he expressly rejected the *Alternative Systems* court's inference that "the client's right to trial *de novo* trumps contractual obligations under binding arbitration" stating that such an inference would render meaningless the MFAA acknowledgement that parties could consent to a form of dispute resolution other than judicial action.[44] Justice Chin rejected *Alternative Systems* as illogical because it provided the client with the means of escaping an agreement to submit disputes to binding arbitration by simply asking for nonbinding arbitration.[45] The court of appeal in the instant case dismissed Justice Chin's analysis, instead choosing to follow the decision in *Alternative Systems*, and found that clients have the "right to trial *de novo* after nonbinding arbitration under the MFAA even when they have signed prospective waivers of trial after arbitration[;]" thus, "the MFAA trumps the CAA" in those situations.[46]

The court then looked directly to the statutory language of the MFAA.[47] The court found that the MFAA, when invoked, provided automatic stays for actions or other proceedings, including binding arbitration, but that such proceedings would move forward once MFAA arbitration was completed.[48] The court then rejected Schatz's argument that the MFAA disallows binding arbitration, stating that the MFAA "does not foreclose the possibility that, under a general agreement between the parties, the *nonbinding* MFAA process should be followed by *binding* arbitration, rather than by lawsuit."[49] The court also recognized that the MFAA provides for a trail following the MFAA arbitration, but does not confer "immunity from valid defenses, such as the existence of a contractual obligation to arbitrate."[50]

Finally, the court considered whether the MFAA impliedly

42 *Id.*
43 *Id.*
44 *Id.* at 1116–17 (italics added).
45 *Id.* at 1117.
46 *Id.* (citing Schatz v. Allen Matkins Leck Gamble and Mallory LLP, 146 Cal.App.4th 674 (2007)) (italics added).
47 *Id.* at 1118.
48 *Id.*
49 *Id.* at 1119 (emphasis in original).
50 *Id.*

repealed the CAA.[51] The court first established that "[a]ll presumptions are against a repeal by implication" and that an implied repeal is only found where statutes conflict such that no harmony can be achieved.[52] The court found that the MFAA could not possibly repeal the CAA because the two acts do not govern the same subject matter—the MFAA covers "nonbinding arbitration that the parties did not agree to in advance" and the CAA covers "binding arbitration agreed to in advance."[53] The court also acknowledged that the statutes may be reconciled because each creates a different type of arbitration, both of which may be given effect.[54] The MFAA creates a nonbinding arbitration; if the arbitration is unsuccessful, the MFAA has fulfilled its role and the parties may pursue other proceedings including judicial action or binding arbitration, to resolve the dispute. In the event the parties selected binding arbitration, or contracted to such in advance, the CAA would apply.[55] The court identified two anomalies that would be created by interpreting the MFAA to repeal the CAA: (1) clients would be able to evade their agreements to arbitrate by requesting and completing MFAA nonbinding arbitration, thus making a charade out of MFAA arbitration just to get to trial, and (2) attorneys could evade their agreements to arbitrate if their clients requested arbitration under the MFAA, thus a client might not choose to invoke their MFAA rights because of the chance that the nonbinding arbitration might fail, and the attorney would proceed to trial instead of the agreed upon binding arbitration.[56]

Holding

The court held that "the MFAA does not stand as an obstacle to the enforcement of a valid agreement to arbitrate pursuant to the CAA."[57]

Legal Significance

The decision establishes that the MFAA and CAA are designed to work together. The MFAA protects, in the form of nonbinding arbitration with the potential for trial *de novo*, clients who find themselves engaged in fee disputes with their attorney. Meanwhile, the CAA protects the arbitration agreements entered

51 *Id.*
52 *Id.*
53 *Id.* at 1120.
54 *Id.*
55 *Id.*
56 *Id.* at 1120–21.
57 *Id.* at 1121.

into by both client and attorney. When the MFAA has fulfilled its role, the CAA takes over.