ARBITRATION ADVISORY

2011-02

STATUTE OF LIMITATIONS FOR FEE ARBITRATIONS

Replaces and Supercedes Arbitration Advisory 1996-02

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INTRODUCTION

Some parties in fee arbitrations have asserted that such proceedings, when initiated by the client, are subject to the one year statute of limitations set forth in Code of Civil Procedure ("CCP") Section 340.6. The law in this area is not as clear as could be desired. This Advisory provides the opinion of the State Bar's Committee on Mandatory Fee Arbitration to assist arbitrators and to provide guidance in those cases where the statute of limitations is asserted as a defense.

WHEN MAY A STATUTE OF LIMITATIONS DEFENSE BE RAISED IN FEE DISPUTES SUBJECT TO ARBITRATION UNDER BUSINESS AND PROFESSIONS CODE SECTION 6200 ET SEQ.?

The statute of limitations may present a jurisdictional question for the arbitrator. A claim which is clearly time barred is not subject to fee arbitration. Business and Professions Code (Bus. & Prof. Code) Section 6206 provides that arbitration may not be commenced if a civil action requesting the same relief would be barred by any applicable statute of limitations. There is a limited exception to this rule, allowing arbitration to be commenced by a client, after the statute of limitations would otherwise have expired, if it follows the filing of a civil action by the attorney.

Two things are therefore clear:

(1) A Section 6200 arbitration is subject to the defense of the statute of limitations in the same way that a civil action for the same relief would be; but

(2) The filing of a lawsuit by the attorney against the client revives the client's right to seek fee arbitration under Section 6200 et seq., even after the statute of limitations has run.

Therefore, the first step in the analysis as to whether a fee arbitration is barred by the statute of limitations would be to determine whether the arbitration was initiated in response to the filing of a civil action by the attorney. If that is the case, Bus. & Prof. Code Section 6206 makes it clear that the arbitration is not barred, and any assertion of the statute of limitations by the attorney must be denied.

SHOULD THE ARBITRATOR RAISE THE STATUTE OF LIMITATIONS ISSUE IF IT HAS NOT BEEN ASSERTED BY ONE OF THE PARTIES?

The statutory scheme under Bus. & Prof. Code Section 6206 expressly states that the arbitration "may not be commenced" if it is time-barred. The fee arbitration procedure is not available to parties if the limitations period has run out (unless the arbitration is initiated in response to the attorney's civil suit).

The California Mandatory Fee Arbitration Program was established by the Legislature in 1979 by the adoption of Business & Professions Code sections 6200, et seq. In enacting the Program, the Legislature noted that disputes concerning legal fees were the "most serious problem between members of the bar and the public." The Legislature also noted that there was a "disparity in bargaining power in attorney fee matters which favors the attorney in dealings with infrequent consumers of legal services" and that "many clients could not afford hiring additional counsel to litigate fee disputes in civil courts." The California Supreme Court also has referred to the MFA Program as one that provides certain "client protections." *Aguilar v. Lerner* (2004)31 Cal.4th 974, 983, 987.

The statute of limitations is normally an affirmative defense which must be raised by a party. The general rule is that an affirmative defense is waived if it is not raised [Getz v. Wallace (1965) 236 C.A.2d 212, 213]. However, the public policy behind mandatory fee arbitration is “to alleviate the disparity in bargaining power in attorney fee matters which favors the attorney by providing an effective, inexpensive remedy to a client which does not necessitate the hiring of a second attorney.” (*Alternative Systems v. Carey* (1998) 67 C.A.4th 1034, 1043; *Manatt, Phelps, Rothenberg & Tunney v. Lawrence* (1984) 151 Cal.App.3d 1165, 1174-1175; *Schatz v. Allen Matkins Leck Gamble & Mallory* LLP (2009) 45 Cal.4th 557, 567.) As a result, MFA matters do not have pleadings that strictly frame the issues as in civil litigation, and special defenses, such as the statute of limitations, typically are not raised by clients who are unrepresented at the hearing and unfamiliar which technical legal defenses. The Committee

therefore believes that it is permissible for the arbitrator to raise this issue sua sponte if it is apparent from the request for arbitration, response, materials presented, and testimony of the parties and any other witnesses.

WHICH STATUTE OF LIMITATIONS GOVERNS AT FEE ARBITRATIONS?

It has traditionally been viewed that attorney-client fee disputes are subject to the same statutes of limitations as other types of contractual disputes. These would include two years for breach of oral contract under CCP Section 339(1); two years for money had and received under CCP Section 339(1); four years for breach of written contract under CCP Section 337(1), and four years for an account stated or open book account under CCP Section 337(2). In addition, these statutes of limitations could be tolled for up to two years if the person entitled to bring the action is imprisoned on a criminal charge at the time the cause of action accrued under CCP Section 352.1.

At first blush, it would seem relatively simple to analyze which statute of limitations might apply, based upon a determination of whether there is a written contract, an oral contract, an open book account, common count for quantum meruit and similar theories of recovery.

This analysis has become more complicated by developments in the law relating to professional negligence, and the possible application of CCP Section 340.6. Section 340.6 generally provides for a one year statute of limitations from the date of discovery (with certain exceptions for tolling). On its face CCP Section 340.6 applies to any "action against an attorney for a wrongful act or omission, other than for actual fraud." The issue becomes a substantial concern in fee arbitrations if the fee dispute is viewed as one which arises out of the "wrongful act or omission" of an attorney. Consider the following issues:

(a) Is an attorney's breach of the fee contract, in the context of a fee dispute, a wrongful act or omission?

(b) Is an attorney's failure to refund an unearned fee or retainer deposit a wrongful act or omission?

(c) Is a fee arbitration to recover an unconscionable fee [Rule 4-200 of the Rules of Professional Conduct] based upon an attorney's wrongful act or omission?

(d) Does an attorney have a four year statute to recover an unpaid fee under a written contract, while the client has only one year to seek to recover an unearned or unconscionable fee?

(e) Does CCP §340.6 impose the one year statute on fee arbitrations?

It has long been the law that a claim of professional negligence against an attorney is both

a tort and a breach of contract [*Neel v. Magana, Olney, Levy, Cathcart & Gelfand* (1971) 6 C.3d 176, 181]. Two Court of Appeal decisions support the conclusion that claims against an attorney in a civil lawsuit for malpractice, pled as a breach of contract, are subject to CCP Section 340.6 [*Southland Mechanical Constructors Corp. v. Nixen* (1981) 119 C.A.3d 417, 431; *Levin v. Graham & James* (1995) 37 C.A.4th 798].

In *Levin v. Graham & James*, one of the allegations of legal malpractice was that the attorney collected "unconscionable fees for professional services." The Court of Appeal determined that Levin's complaint was one sounding in legal malpractice and therefore barred by the provisions of CCP Section 340.6.

> "Indeed, for any wrongful act or omission of an attorney arising in the performance of professional services, an action must be commenced within one year after the client discovers or through the use of reasonable diligence should have discovered the facts constituting the wrongful act or omission. In all cases other than actual fraud, whether the theory of liability is based on the breach of an oral or written contract, a tort, or a breach of fiduciary duty, the one year statutory period applies (*See Southland Mechanical Constructors Corp. v. Nixen* (1981) 119 C.A.3d 417) [*Levin, supra*, 37 C.A.4th at 805].

Some attorneys have asserted that *Levin* establishes a one year statute of limitations for any client seeking to resolve a fee dispute by way of fee arbitration under the applicable provisions of the Business and Professions Code. The Committee does not believe that this is a reasonable interpretation of the *Levin v. Graham & James* decision, nor that CCP Section 340.6 is applicable to the fee arbitration process. The Committee is concerned about fundamental fairness and equity if attorneys are given a longer period of time in which to pursue a claim to recover fees than a client has to initiate a claim to determine a reasonable fee or to recover an unconscionable fee.

This Committee interprets both *Southland* and *Levin* to stand for the proposition that CCP §340.6 applies to contractual disputes only where the gravamen of that litigation is the claim of professional negligence. We have found no cases in California which hold that a fee arbitration under the statutory scheme established by Bus. & Prof. Code Section 6200 et seq. is subject to the one year statute of limitations under CCP §340.6. Neither *Levin* nor *Southland* dealt with a fee arbitration. Neither case dealt with a pure fee dispute. The gravamen of both claims was professional negligence. Nevertheless, one aspect of Levin's claim was the recovery of an "unconscionable fee," and the *Levin* court did conclude that charging an excessive fee can be the basis of a legal malpractice claim subject to the one year statute. In summary, the Committee recommends that Section 340.6 should not be applied to fee arbitration proceedings conducted under Bus. & Prof. Code Sections 6200 et seq.

The basis for this conclusion is primarily an analysis of the scope of the statutory scheme which mandates the fee arbitration process. Bus. & Prof. Code Section 6200(b) expressly provides that: "This article shall not apply to ...

(2) Claims for affirmative relief against the attorney for damages or otherwise based upon alleged malpractice or professional misconduct, except as provided in subdivision (a) of Section 6203."

Bus. & Prof. Code Section 6203(a) provides that evidence of professional misconduct or negligence may only be received for a limited purpose, and the arbitrators may not award affirmative relief in the form of damages or offset. Consequently, the fee arbitration statutes do not allow the recovery of damages from the attorney. Applying this analysis to the language of Bus. & Prof. Code Section 6206, the fee arbitration "may not be commenced under this article if a civil action requesting the same relief would be barred" by any applicable statute of limitations.

It is the opinion of the Committee that a claim for fee arbitration under Bus. & Prof. Code Section 6200 does not seek the same relief as a malpractice claim or an action for malpractice pled as a breach of contract. Under the limitations of Bus. & Prof. Code Sections 6200(b)(2), and 6203(a), the arbitrators cannot award damages or other affirmative relief on any theory sounding in legal malpractice or professional misconduct. By definition, fee arbitration does not seek the same relief as a claim which may be barred under CCP Section 340.6. The Committee concludes that, based upon the statutory analysis of Bus. & Prof. Code §6200 et seq., in the absence of legislative guidance or a clear interpretation from the courts, CCP Section 340.6 should not be applied to fee arbitrations under the auspices of the Mandatory Fee Arbitration Program.

Open Book Accounts and Accounts Stated. Following the enactment of Bus. & Prof. Code §6148 requiring written contracts for services (fee agreements) where it is reasonably foreseeable that the fee will exceed $1,000, except in specific instances, the likelihood of a matter without a written agreement qualifying as anything other than an oral agreement is extremely unlikely. The exceptions to the requirement for written fee agreements are spelled out in Section 6148(d):

"(1) Services rendered in an emergency to avoid foreseeable prejudice to the rights or interests of the client or where a writing is otherwise impractical.

(2) An arrangement as to the fee implied by the fact that the attorney's services are of the same general kind as previously rendered to and paid for by the client.

(3) If the client knowingly states in writing, after full disclosure of this section, that a writing concerning fees is not required.

(4) If the client is a corporation."

Subsection 6148(c) provides that: "Failure to comply with any provision of this section renders the agreement voidable at the option of the client, and the attorney shall, upon the agreement being voided be entitled to collect a reasonable fee."

If the implied agreement (open book or account stated) is voided pursuant to Bus. & Prof. §6148 then the two year statute for oral agreements would apply and the basis for computing the fee would be quantum meriut.. (*Iverson, Yoakum, Pampiano & Hatch v. Berwald* case (1999) 76 Cal.App.4th 990. 996 [Where services have been rendered under a contract which

is unenforceable because not in writing, an action generally will lie upon a common count for *quantum meruit*; the statute of limitations for quantum meruit claims is two years (see Code Civ. Proc., §339)].) Thus, before making a determination to consider the fee agreement voided (See, Arbitration Advisory 1994-04 Voidability of Fee Agreements) the arbitrator should evaluate whether voiding the agreement would result in the client's fee arbitration claim being barred by the shorter two year statute of limitations.