

**THE STATE BAR OF CALIFORNIA STANDING COMMITTEE ON
PROFESSIONAL RESPONSIBILITY AND CONDUCT**

ARBITRATION ADVISORY 2020-01

Replaces and Supersedes Arbitration Advisory 1993-01

INTRODUCTION

California Business and Professions Code sections 6200-6206 confer jurisdiction upon Mandatory Fee Arbitration (MFA) arbitrators to consider and make awards concerning disputes over fees, costs, or both, that are charged to a client in connection with professional services rendered by an attorney. The purpose of an arbitration advisory is to provide guidance to MFA arbitrators regarding disputes or issues that may arise in connection with MFA arbitrations.

This arbitration advisory is intended to summarize existing law and to provide guidance to Mandatory Fee Arbitration arbitrators on the awarding of interest as part of the fee arbitration award (“Award”), including when and how much interest may be awarded.

ANALYSIS

1. May pre-award interest be awarded as part of the Award? Yes.

Business and Professions Code sections 6200-6206 provide for the arbitration of fee disputes between attorneys and their clients. Attorneys are required to arbitrate fee disputes when timely requested by the client (Bus. & Prof. Code § 6200(c)). The arbitrator(s) may resolve all disputes concerning fees, costs, or both.

The fee arbitration statutes do not mention an award of interest. However, they likewise do not preclude an award of interest. The statutes specify circumstances when fee arbitration is not available (e.g., Bus. & Prof. Code § 6200(b)(3) [when fees are awarded pursuant to statute or court order]) and when fee arbitration precludes the recovery of certain types of damages (e.g., Bus. & Prof. Code § 6203(a) [attorneys’ fees cannot be awarded to either party]). Accordingly, the availability of interest in arbitration is governed by the same legal principles that govern the award of interest in a court proceeding.

The basic standards governing the availability of prejudgment interest are as follows: “Every person who is entitled to recover damages certain, or capable of being made certain by calculation, and the right to recover which is vested in him upon a particular day, is entitled also to recover interest thereon from that day. . .” (Civil Code § 3287(a)). “The detriment caused by the breach of an obligation to pay money only, is deemed to be the amount due by the terms of the obligation, *with interest thereon.*” (Civil Code § 3302 [italics added]).

While a client may obtain pre-award interest whenever it meets the statutory standard, an attorney may not ethically charge interest or impose late charges on past-due fees and costs unless the client has given its informed consent to the charging of interest and to the rate of interest to be charged so long as the rate is not unconscionable. (Cal. State Bar Form. Opn. No. 1980-53; ABA Form. Opn. No. 388 (1974); Los Angeles County Bar Assn. Formal Opn. Nos. 370 [interest on unpaid fees and costs], 374 [interest on unpaid fees], and 499 [interest on advanced costs]; Bar Association of San Francisco Ethics Opn. No. 1970-1; San Diego County Bar Assn. Form. Opn. 1983-1.) Normally, that consent will be given in the fee agreement or an amendment thereto.

2. May pre-award interest be awarded regardless of the existence of a written contract?

The client's right to recover interest for breach of contract is not predicated on the existence of a written contract. Accordingly, even in the absence of a written agreement providing for pre-award interest, the client may recover interest whenever the principal amount owed to the client is readily ascertainable—that is, “certain, or capable of being made certain by calculation” within the meaning of Civil Code section 3287. (*Collins v. City of Los Angeles* (2012) 205 Cal.App.4th 140, 150-151 [139 Cal.Rptr.3d 880]; *Macomber v. State of California* (1967) 250 Cal.App.2d 391, 400 [58 Cal.Rptr. 393].) This test “is not an easy one to apply.” (*Marine Terminals Corp. v. Paceco, Inc.* (1983) 145 Cal.App.3d 991, 995 [193 Cal.Rptr. 687].) The basic rule though, is that if the principal amount owed to the client can be calculated from the terms of the contract itself or from other evidence, such as invoices or billing statements rendered by the attorney, and does not depend on the resolution of factual disputes concerning the amount owed, interest should be awarded. (*Collins v. City of Los Angeles, supra*, at pp. 150-151; *Macomber v. State of California, supra*, at p. 401.)

The lawyer's right to recover pre-award interest, in contrast, depends on there being a statutorily complying written contract providing for the attorney to recover pre-award interest and specifying the rate. (Cal. State Bar Form. Opn. No. 1980-53.) If a lawyer satisfies the requirement that the attorney has a contract with the client which provides for pre-award interest, then the lawyer may recover pre-award interest even though the client disputes liability so long as the amount sought by the attorney (whether reflected in the terms of the contract, the lawyer's bills, or otherwise) are sufficient to render the amount sought reasonably certain and capable of calculation. (*Collins v. City of Los Angeles, supra*, at pp. 150-151 [damages are certain or capable of being made certain by calculation, or ascertainable, for purposes of Civil Code section 3287 if the defendant actually knows the amount of damages or could calculate that amount from information reasonably available to the defendant].)

In contrast, where the amount of damages is unliquidated, disputed, and depends on the fact-finders' resolution of conflicting evidence, pre-award interest is not available. (*Fitzsimmons v. Jackson* (9th Cir. (BAP) 1985) 51 B.R. 600, 612-613 [court denied prejudgment interest to attorney where the basis of the attorney's action to recover fees was quantum meruit rather than existence of a valid fee agreement]; *Parker v. Maier Brewing Company* (1960) 180 Cal.App.2d 630, 634 [4 Cal.Rptr. 825] [where there is no express contract and action is in

quantum meruit to recover reasonable value of services, prejudgment interest is not recoverable]; *Garrie v. McCauley* (1958) 163 Cal.App.2d 273, 276 [328 P.2d 1013] [attorney not entitled to prejudgment interest where fee claim was based on an implied contract and the amount could not be determined except by evidence of the reasonable value of the services rendered].) Thus, where the lawyer's or client's right to recover is based upon the outcome of a "reasonable fee" analysis, in most cases, the amount owed is not and cannot be ascertainable until the arbitrator(s) determine the reasonable value of the attorney's services. Similarly, where the client presents evidence supporting any significant reduction in the amount the attorney claims is owed the value of the final fee is only ascertained after the outcome of the hearing is known. In these situations, no pre-award interest may be included in the award to either party because the amount owed will only become "ascertainable" when the award is issued. (Civ. Code § 3287(a).)

3. What rate of pre-award interest should be used and how should it be calculated?

When there is no written agreement that specifies a statutory rate of interest, the arbitrators shall award simple interest at the rate of 10 percent per annum on the amount of the award (or the then-applicable statutory rate, if different) from the date of breach. (Code Civ. Proc. § 3289(b).)

When there is a written agreement that specifies the rate of interest, then the rate set forth in the contract shall apply. (Civ. Code § 3289(a).) However, the rate of interest charged or the late penalty imposed must not be illegal or amount to an "unconscionable" fee. (See, California Rule of Professional Conduct 1.5(a); see also, Cal. State Bar Form. Opn. No. 1980-53.)

Pre-award interest should be awarded from the date of breach through the date of the Award. (Code Civ. Proc. § 3289.) The date of breach is a question of fact primarily based on when the obligation was due. Oftentimes, the written fee agreement will provide when the obligation is due or on what date a breach is deemed to occur. The date of breach may also vary depending on when the bills are presented to the client. For instance, if the engagement letter provides for interest from the date of the invoice, but the attorney's practice is to send the invoice to the client on some later date, then the calculation cannot begin until the later date. Additionally, the burden is on the attorney to establish the relevant dates for this calculation.

In calculating interest, the obligation should bear simple interest unless the parties have agreed that interest should be compound. Under California law, the general rule is that "compounded interest is impermissible unless specifically authorized by statute or by stipulation of the parties." (*State of California v. Day* (1946) 76 Cal.App.2d 536 [173 P.2d 399].) If the fee agreement expressly provides for compound interest, that should be scrutinized for unconscionability.

To calculate pre-award interest on an award bearing simple interest, simply use the following formula:

$$\text{(Amount of Award)} \times \text{(Applicable Interest Rate)} \div 365 \text{ (days in a year)} \times \text{(number of days elapsed between the Date of Breach and the Date the Award is signed)}$$

Example 1: Assume that the facts in a fee dispute demonstrate that a client failed to timely pay \$5,000 (Amount of the Award) since March 1 (Date of Breach) and that the valid and enforceable fee agreement states that any unpaid balance shall accrue 5 percent simple interest (Applicable Interest Rate). Further assume that the arbitration award is to be signed on December 1 of the same year (Date of Award). From the foregoing facts, the equation would look as follows.

$$\$5,000 \text{ (Amount of the Award)} \times .05 \text{ (number value of 5\%)} \div 365 \text{ (days in a year)} \times 275 \text{ (number of days elapsed between the Date of Breach on March 1 and the Date the Award is signed on December 1)} = \$188.36 \text{ (Amount of Pre-Award Interest)}$$

Example 2: Assume that the facts of a fee dispute demonstrate that the client is entitled to pre-award interest for some amount wrongfully withheld by the attorney. For example, assume that in a personal injury case, the gross contingency fee agreement states that the attorney shall be paid 30 percent of any settlement obtained before trial, or 40 percent of any settlement or judgment obtained after trial actually starts. Now assume that the case settles two months before the first trial date for \$100,000 and that on March 1, 2016, the attorney declares that notwithstanding the terms of the fee agreement, he is entitled to a \$40,000 fee and deposits the disputed \$10,000 into his trust account pending resolution of the client's fee dispute. Assume further that the facts of the resulting arbitration demonstrate that the attorney wrongfully withheld the \$10,000 (Amount of the Award) since March 1, 2016 (Date of Breach). Also, assume that the applicable legal interest rate on the date of the breach was 10 percent (see Civ. Code § 3289(b) [Applicable Interest Rate]). Lastly, assume that the arbitration award is to be signed on June 1, 2017 (Date of Award). From the foregoing facts, the calculation would look as follows.

$$\$10,000 \text{ (Amount of the Award)} \times .10 \text{ (number value of 10\%)} \div 365 \text{ (days in a year)} \times 457 \text{ (number of days elapsed between the Date of Breach on March 1, 2016 and the Date the Award is signed on June 1, 2017)} = \$1,252.05 \text{ (Amount of Pre-Award Interest)}$$

4. Post-Award Interest

Unlike the foregoing considerations regarding pre-award interest, an award of post-award simple interest is required on all awards, in the amount of the statutory rate of interest on all judgments, which commences accruing from the 30th day after service of the award. (Guidelines and Minimum Standards for the Operation of the Mandatory Fee Arbitration

Programs No. 14.) The requirement to award post-award interest in all cases serves two important purposes. First, it represents fair compensation to the prevailing party for the failure of the other party to pay the award promptly. Second, where the award requires the attorney to make a refund of some or all of the fee already paid, the award of post-award interest provides a valuable tool to the State Bar and the client when enforcement procedures become appropriate under Business and Professions Code section 6203(d). (Code Civ. Proc. § 685.010, Minimum Standard 16).

CONCLUSION

Consistent with California law, the arbitrator(s) may award clients pre-award interest from the date of breach through the date of the Award in cases where damages are readily ascertainable. An award of pre-award interest to the attorney requires both that the attorney meet the statutory standard and that the attorney prove a contract in which the client has consented to the charging of interest and the rate to be charged. When the determination of the principal amount owed requires the resolution of disputed issues of fact, then interest is unavailable on the disputed portion of the principal. Unless the written agreement provides for compounding of interest, the obligation should only bear simple interest. The interest rate should be 10 percent (or the then-applicable statutory rate) unless there is a written agreement which provides otherwise, and in such circumstance, the written contract rate should apply, unless the interest charged is illegal or unconscionable. Both lawyer and client are entitled to statutory post-award interest on the amount of any award in their favor.

This arbitration advisory is issued by the Standing Committee on Professional Responsibility and Conduct of the State Bar of California. It is advisory only. It is not binding upon the courts, the State Bar of California, its Board of Trustees, any persons, or tribunals charged with regulatory responsibilities, or any licensee of the State Bar.