

Practice Points

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Law Firm's Refusal to Pay Former Client's Arbitration Fees Subjects It to Litigation

Many law firms include an arbitration clause in the retention agreements that they have with their clients. Such agreements have the same advantages (and disadvantages) that arbitration agreements do in many other settings. Generally speaking, they enable firms to resolve disputes quicker, cheaper, and with less publicity than litigation. But what happens when the client cannot afford to pay its share of the arbitration fees?

Situations where one party cannot or will not pay its share of the arbitration fees arise with some frequency, and the options for addressing this problem are limited. In *Tillman vs. Rheingold, Valet, Rheingold, Shkolnik & McCartney*, a client filed a malpractice suit against her attorneys in federal court, and the firm successfully moved to stay her case and to require her to arbitrate her claims. At some point, however, the client ran out of funds and could not afford to continue to pay her half of the arbitrator's compensation. The arbitrator asked the law firm to pay the client's share, and the law firm refused. Unwilling to work for half-pay, the arbitrator dismissed the case, and the client then moved to lift the stay and resume her malpractice suit. The law firm convinced the district court to dismiss the case, but the Ninth Circuit reversed.

The Ninth Circuit affirmed the part of the district court opinion that refused to dismiss the client's case under Rule 41(b). It agreed that such dismissal is a "harsh penalty" that should not be employed where, as here, the client was willing to obey the district court's order to arbitrate but was unable to pay the expenses of the arbitration and therefore was not culpable in her failure to obey a court order.

However, the Ninth Circuit disagreed with the district court's ruling that the court had no authority to allow the client's lawsuit to resume. The Ninth Circuit noted that section 3 of the Federal Arbitration Act (FAA) requires courts to stay litigation "until such arbitration has been had in accordance with the terms of the [arbitration] agreement." The court interpreted this phrase to be satisfied.

In this regard, the court stated that nothing in the FAA required dismissal in a situation where, as here, the arbitration had gone as far as it could, the arbitration had not been decided on the merits or otherwise resulted in an award, and the arbitration had been terminated in accordance with the arbitration rules because the plaintiff truly could not afford to pay the ongoing arbitration fees. The court held that district courts have an obligation to decide the cases before them "absent a firm basis for declining to do so." *Id.* at 13. Accordingly, it remanded the case with instructions to permit the malpractice case to go forward.

There are two points that are central to this decision. First, the client legitimately could not afford to pay the ongoing arbitration fees and proved that to the district court's satisfaction. Indeed, the

Ninth Circuit noted that if the client could afford to pay the arbitration fees but refused to do so, the district court “most probably” (and properly) would have dismissed her complaint under Rule 41(b) for failing to comply with the district court’s order to arbitrate.

Secondly, the law firm could have avoided further litigation if it had paid the client’s share of the arbitrators’ compensation and allowed the arbitration to be decided on the merits. Indeed, the law firm could have asked the arbitrator to allocate the arbitration fees evenly to each side in the eventual award. Instead, the law firm played hard ball and lost the opportunity to arbitrate its client’s malpractice claims.

Keywords: alternative dispute resolution, adr, litigation, legal malpractice, Rule 41(b), failure to pay arbitration fees or expenses, stay of litigation, dismissal

—[Mitchell L. Marinello](#), *Novack and Macey LLP, Chicago, IL*