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When conduct or impoverishment waives the right to compel arbitration

THE LAW AND SELECTED CASE EXAMPLES OF CONDUCT THAT WAIVE THE RIGHT TO COMPEL ARBITRATION.

Waiver generally denotes relinquishing a known right or losing a right due to a party's failure to perform a required act. (See *Engalla v. Permanente Medical Group, Inc.*, (1997) 15 Cal.4th 951, 982-983.) For example, certain conduct by a party seeking to compel an arbitration agreement can create an opportunity for the opposing party to move the court to rule that such conduct waived its right to arbitration. More specifically, the California and federal rules are:

California*:* Code Civ. Proc. § 1281.2, subdivision (a) states:

> On petition of a party to an arbitration agreement alleging the existence of a written agreement to arbitrate a controversy and that a party to the agreement refuses to arbitrate that controversy, the court shall order the petitioner and the respondent to arbitrate the controversy if it is determined that an agreement to arbitrate the controversy exists, unless it is determined that:
> 1. The right to compel arbitration has been *waived* by the petitioner.

Federal: There is no specific code section defining waiver for federal actions. But in the recent case of *Armstrong v. Michaels Stores, Inc.* (9th Cir. 2023) 59 F.4th 1011, 1015, the court states that the federal waiver rule requires that "the party asserting waiver must demonstrate: (1) knowledge of an existing right to compel arbitration and (2) intentional acts inconsistently with that existing right."

Note: Until recently, federal *and* state courts required proof of prejudice to the party seeking arbitration waiver. As explained later in this article, *United States Supreme Court in Morgan v. Sundance* (2022) 142 S.Ct. 1708, held that prejudice is not required to prove waiver for federal cases. The California Supreme Court is reviewing California's prejudice requirement in *Quach v. California Commerce Club* (2022) S275121, 297 Cal.Rptr.3d 592.

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
July 2023

Essential factors in establishing waiver of a contractual right to arbitration

In *Saint Agnes Medical Center v. PacifiCare of California* (2003) 31 Cal.4th 1187, the California Supreme Court set forth factors a trial court can consider in evaluating an arbitration waiver *by the party seeking enforcement* of the arbitration agreement. Considerations of waiver are whether:

- The party's actions are inconsistent with the right to arbitrate;
- The litigation machinery has been substantially invoked, and the parties were well into the preparation of a lawsuit before notification of an intent to arbitrate;
- The party either requested arbitration enforcement close to the trial date or delayed seeking arbitration enforcement for an extended period before seeking a stay;
- The party seeking arbitration filed a counterclaim without asking for a stay of proceedings;
- Important intervening steps, such as taking advantage of judicial discovery procedures not available in arbitration, had taken place; or
- The delay in seeking arbitration enforcement affected, misled, or *prejudiced* the opposing party.

Note: The *Saint Agnes* holding required proof of *prejudice* to the party seeking a waiver of arbitration enforcement by the conduct of the party seeking to compel the arbitration agreement: "The question of prejudice, however, is 'critical in waiver determinations.'" (*Id.* at p. 1203.) See the next section on prejudice.

Must a party seeking an arbitration waiver prove prejudice?

California and federal court decisions have long required a party seeking a waiver of arbitration enforcement to prove prejudice caused by conduct of the party seeking an order to arbitrate. For example, in *Saint Agnes Medical Center,* 31 Cal.4th at pp. 1203-1205, the Court explained that, to find waiver, both California and federal case law *requires* the presence of prejudice incurred by the party objecting to a motion to compel arbitration.

Relying on *Saint Agnes Medical Center,* the appellate court in *Quach v. California Commerce Club* (2022) 78 Cal.App.5th 470, required evidence of *prejudice* to the party seeking waiver and overturned the trial court's finding of arbitration waiver where prejudice to the objecting party was not found. Shortly after the *Quach* decision, the United States Supreme Court in *Morgan v. Sundance, Inc.* held that, under federal law, *prejudice* was *not* a requirement to prove waiver of a right to arbitrate.

The *Morgan* court reasoned that since prejudice is not a requirement to prove waiver in *any other* contract action, it should not be more challenging to prove waiver in arbitration matters. "[F]ederal policy is about treating arbitration contracts like all others, not fostering arbitration." *(Id.* at p. 1713.)

In essence, the U.S. Supreme Court held that the burden to prove waiver of arbitration should be the same as the burden for establishing waiver in any other contractual context. That is, the burden to prove arbitration waiver should *not* be heavier than the burden to prove any other breach of contract.

Prior to the *Morgan* holding, the Ninth Circuit required proof of prejudice to the party opposing enforcement of the arbitration agreement before finding conduct waiver by the party seeking arbitration enforcement. Following *Morgan*, the Ninth Circuit eliminated the prejudice requirement in *Armstrong v. Michaels Stores, Inc.* (9th Cir. 2023) 59 F.4th 1011, holding that prejudice to the opposing party was not required to prove that the party seeking enforcement of the arbitration agreement waived its contractual enforcement right. The *Armstrong* court, however, did not find a delay of about one year inconsistent with the right to seek arbitration of the dispute and upheld the compelling of the arbitration.

Spurred by the *Morgan* holding, on August 24, 2022, the California Supreme Court granted review of *Quach* S275121 (297 Cal.Rptr.3d 592). At this writing, a hearing before the Court is pending.

A sampling of cases holding waiver of arbitration rights

The following are examples of cases finding *prejudice* to a party claiming waiver and objecting to compelling of the arbitration agreement:

California:

1. Bad-faith delaying tactics. *Engalla v. Permanente Medical Group, Inc*., (1997) 15 Cal.4th 951;
2. During a six-month delay, the defendant filed two demurrers, contested discovery requests, and engaged in discovery scheduling. *Adolph v. Coastal Auto Sales, Inc.* (2010) 184 Cal.App.4th 1443;
3. An employer's substantial delay (17 months) in demanding arbitration required extensive discovery hours, payment of jury fees, appearance at case management conferences, and jury demand was held to be a waiver of arbitration rights. *Oregel v. PacPizza, LLC* (2015) 201 Cal.App.4th 342;
4. In a wrongful termination action, the employer filed an ill-fated summary judgment motion, attempted to delay trial with several motions, and motioned to compel arbitration on the eve of trial. *Diaz v. Professional Community Management, Inc.* (2017) 225 Cal.Rptr.3d 39;
5. Where affirmative defense fails to allege an arbitration provision. *Guess?, Inc. Superior Court* (2000) 79 Cal.App.4th 533, 558;
6. An employer failed to compel a contractual arbitration provision until after a Labor Commission order. *Fleming Distribution Company v. Younan* (2020) 49 Cal.App.5th 73.

(For a listing of cases with varied time delays holding waiver of arbitration rights, see *Oregel v. PacPizza, L.L.C.* (2015) 201 Cal.App.4th 342, 361.)

Ninth Circuit:

1. Cosmetology students seeking enforcement of the Fair Labor Standards Act were found to be *prejudiced* by the defendant's 17-month delay in asserting

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
July 2023

its contractual right to arbitrate and requiring unnecessary special federal rules to be followed by plaintiffs because of the delay. *Martin v. Yashuda* (9th Cir. 2016) 829 F.3d 118;
2. After the original motion to arbitrate was withdrawn, that party sought discovery, which created *prejudicial expenses* for the opposing party. *Newirth v. Aegis Senior Communities, L.L.C.* (9th Cir. 2019) 931 F.3d 935.

Cases where *prejudice* was *not* found and waiver denied

The following cases are examples of waiver denial because *prejudice* to the party seeking waiver was not found:

California:

1. Where no *prejudice* to the party seeking a waiver was found due to the delay or other conduct of the party seeking enforcement of the arbitration agreement. (See subsection of discussion of "Privilege.") *Saint Agnes Medical Center v. PacifiCare of California* (2003) 31 Cal.4th 1187, following the case of *Sobremonte v. Superior Court (Bank of America Nat. Trust and Sav. Ass'n.)* (1998) 61 Cal.App.4th 980, 992;
2. No prejudice where discovery conducted during the pendency of a court proceeding produces information that would have been available if discovery had been conducted in arbitration. *Iskanian v. C.L.S. Transportation Los Angeles, L.L.C.* (2014) 59 Cal.4th 348, 378.

Ninth Circuit:

1. Lack of knowledge by an unrepresented defendant of a right to arbitration for nearly a year and adverse discovery orders were insufficient to show plaintiff suffered prejudice by the delay. *Britton v. Co-op Banking Group* (9th Cir. 1990) 916 F. 2d 1405;
2. A three-and-a-half-year delay in seeking arbitration with substantial discovery was not prejudicial when the parties were awaiting a U.S. Supreme Court ruling. *Fisher v. A.G. Becker Paribas Inc*. (9th Cir. 1986) 791 F. 691.

Filing a court complaint does not prevent the future right to seek a waiver of an opponent's predispute arbitration agreement rights

Merely filing a court complaint for damages is not a waiver of a right to later arbitrate a dispute required under a predispute arbitration agreement. (Code Civ. Proc., § 1281.12.) Section 1281.12 is a tolling provision that preserves the right of a party to petition for arbitration after filing a complaint. (See *Sargon Enterprises, Inc. v. Brown George Ross, L.L.P.* (2017) 15 Cal.App.5th 749 [confirming that a client's court complaint challenging the enforceability of an arbitration agreement in an attorney-client retainer agreement does not forfeit the filing party's right to arbitration].) Also, an employee's *application for retirement benefits* after disciplinary termination is not a waiver of arbitration under a relevant union contract. (*Service Employees International Union Local 1021 v. County of San Joaquin* (2011) 202 Cal.App.4th 44.)

Does the court or arbitrator decide arbitration waivers?

California: Determination of waiver is a question of fact; however, when the facts are undisputed, waiver reference is one of law. (See *Platt Pacific, Inc. v. Andelson* (1993) 6 Cal.4th 307, 319.) In *Iskanian v. C.L.S. Transportation Los Angeles, L.L.C.* (2014) 59 Cal.4th 348, 374-375, the Court states: "In light of the policy in favor of arbitration, waivers are not to be lightly inferred and the party seeking to establish a waiver bears a heavy burden of proof." (See *Williams v. West Coast Hospitals, Inc.* (2022) 86 Cal.App.5th 1054 (review den. Mar. 29, 2023) [holding a court, not an arbitrator, determines waiver when the drafting party fails to pay the required arbitration fees within the statutory 30 days].)

Ninth Circuit: If parties to an arbitration agreement want an arbitrator to decide the question of waiver, "they must place clear and unmistakable language to that effect in the agreement." (*Martin v. Yasuda* (9th Cir. 2016) 829 F.3d 1118, 1124.)

Waiver of arbitration rights when a party cannot pay arbitration fees

A line of cases finds waiver of a predispute arbitration agreement when a party cannot afford the arbitration fees. Many of these cases deal with attorney-client relations and hold the drafting party attorney has the option to: (1) pay the arbitration fees; or (2) waive arbitration and allow the matter to proceed to trial. The cases are:

- *Cinel v. Barna* (2012) 206 Cal.App.4th 1383: Some of the parties could not pay the arbitration fees, and the remaining parties failed to agree to pay the balance of the fees owing. The court held arbitration waived, and the matter was ordered to trial.
- *Roldan v. Callahan & Blaine* (2013) 219 Cal.App.4th 87: In a legal malpractice case, the former client did not have the resources to pay the arbitration costs required by the retainer contract drafted by the attorney defendant. The defendant attorney was given the option to pay the arbitration fees *or* waive arbitration and proceed to trial. *Roldan* was cited with approval in *Jameson v. Desta* (2018) 5 Cal.5th 594, 622.:

> [U]nder California law when a litigant in a judicial proceeding has qualified for *in forma pauperis* status, a court may not consign the indigent litigant to a costly private alternative procedure that the litigant cannot afford and that effectively negates the purpose and benefit of *in forma pauperis* status. In other words, whatever a court's authority may be in general to outsource to privately compensated individuals or entities part or all of the court's judicial duties with respect to litigants who can pay for such private services, a court may not engage in such outsourcing in the case of *in forma pauperis* litigants when the practical effect is to deprive such litigants of the equal access to justice that *in forma pauperis* status was intended to afford.

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
July 2023

• *Tillman v. Tillman* (2016) 825 F. 3d 1069 (9th Cir. 2016): In a matter similar to *Roldan*, the former client lacked the resources to pay arbitration fees, and the arbitrator terminated the arbitration without an award. The District Court ordered the matter to trial as the only way the plaintiff's claims could be adjudicated.

• *Weiler v. Marcus & Millchap Real Estate Investment Services, Inc.* (2018) 22 Cal.App.5th 970: Where the claimant could not continue to pay for a three-party arbitration panel, the court followed *Roldan* and held an indigent party's fundamental right to a judicial forum outweighs the opposition's contractual right to arbitrate the claim. "With the rising costs of arbitration . . . , our decision today ensures those compelled to arbitrate will not, as a result, be inherently disadvantaged." (*Id.* at p. 981.) In footnote 3., the court states in part:

> We seriously doubt parties will purposefully make themselves impecunious to have their cases returned to the courts. Regardless, we are more concerned with deep-pocketed parties leveraging their wealth to deprive their opponents of the right to resolve their disputes than we are with parties choosing to bankrupt themselves as a way out of arbitration and into court. And, under our holding today, a court may not grant relief if the evidence demonstrates a party's financial status is a result of the party's intentional attempt to avoid arbitration.

• *Aronow v. Superior Court (Emergent, L.L.P.)* (2022) 76 Cal.App.5th 868: The court ruled an indigent party to an arbitration is to be compared to a court litigant who proceeds *in forma pauperis*. Each is entitled to have their dispute adjudicated. The defendant law firm was given the same option set out in *Roldan*, allowing the attorney to pay the arbitrator's fee or waive the right to arbitration.

• *Hang v. RG Legacy I, LLC* (2023) 88 Cal.App.5th 1243: An indigent elder left no estate, and neither his successor in interest estate nor family had the necessary assets to proceed with an elder abuse arbitration. The trial court upheld a viable arbitration agreement for elder abuse. But, because of a lack of resources, the arbitration could only proceed if the defendant's elder care facility paid the arbitration fees and costs. "Consistent with *Roldan*, and federal and California arbitration statutes, a party's fundamental right to a forum she or he can afford may outweigh another party's contractual right to arbitrate." (*Id.* at. 1258.)

A waiver of arbitration rights under Code of Civil Procedure sections 1281.97 and 1281.98

Under Code of Civil Procedure sections 1281.97 and 1281.98, if a *drafting* party of a consumer or employment predispute arbitration agreement fails to timely pay arbitration fees within 30 days of the due date, the opposing party has the *option* to petition or move the court to withdraw the claim from arbitration and proceed with court action. Such failure by the drafting party is a material breach and default of the arbitration agreement, thereby waiving the right to arbitrate. (See *Williams v. West Coast Hospitals, Inc.* (2022) 86 Cal.App.5th 1054, 1061 (review den. Mar. 29, 2023).)

The two code sections were effective January 1, 2020, and the following cases have interpreted them:

• The drafting party was ordered to trial when it failed to timely pay the required American Arbitration Association (AAA) fees. (See *Gallo v. Wood Ranch U.S.A., Inc.* (2022) 81 Cal.App.5th 621 [holding sections 1281.97 and 1281.98 did not violate the Federal Arbitration Act, as they encourage prompt access to arbitration rather than being a deterrent to arbitration].)

• A former employee was allowed to withdraw his claim from arbitration and proceed in court when the employer's arbitration fee payment was not paid within the codes' 30-day requirement. (*De Leon v. Juanita Foods* (2022) 85 Cal.App.5th 740).

• *Williams v. West Coast Hospitals, Inc.* (2022) 86 Cal.App.5th 1054, (review den. Mar. 29 2023) held a court, and not an arbitrator, determines waiver when the drafting party fails to pay the required arbitration fees within the statutory 30-day requirement.

• Payment of the arbitrator's fee on the 32nd day after the due date was a material breach that violated the 30-day statutory requirement. (*Espinoza v.* Superior Court (Cetinela Skilled Nursing & Wellness Centre West, L.L.C.) (2022) 83 Cal.App.5th 761.)

An unpublished district court opinion, *Belyea v. Greensky* (October 26, 2022) WL 14965532, is a likely precursor of federal court holdings on the 30-day payment requirement. The court held:

> (1) if the agreement fails to have a *time-of-the-essence* provision regarding arbitration fees, payment of the fees 40 days after receipt of the invoice is not a material breach causing a waiver;
> (2) the Federal Arbitration Act's equal treatment provision requires arbitration agreements to be enforceable, except on a ground for revocation (9 U.S.C., § 2); and
> (3) waiver requires acts inconsistent with the existing right to arbitrate the dispute.
>
> For further reading on the application of sections 1281.97 and 1281.98, see Tilak Gupta, "*When the defendants do not timely pay arbitration fees*," (March 2023), Advocate, pages 90-94. Additionally, practitioners will likely see future predispute arbitration agreements allowing payment deadlines to exceed the 30-day statutory time limit.

Conclusion

There can be no better conclusion to this article on arbitration waiver than the final paragraph of the appellate court's upholding of a defendant's arbitration waiver in the matter of *Oregel v. PacPizza,*

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
July 2023

L.L.C. (2015) 237 Cal.App.4th 342, 362:

> We are [loath] to condone conduct by which a defendant repeatedly uses the court proceedings for its own purposes ..., all the while not breathing a word about the existence of an arbitration agreement, or a desire to pursue arbitration.... We note that "'the 'bad faith' or 'willful misconduct' of a party may constitute a waiver and thus justify a refusal to compel arbitration." [Citations.] Although the trial court made no express finding of bad faith, the tone of its ruling is suggestive of such a finding and, had it been made, sufficient evidence would have supported the finding. True, California has a strong public policy in favor of arbitration. But that public policy is founded upon the notion that arbitration is a "'speedy and relatively inexpensive means of dispute resolution.'" [Citation.] That goal was frustrated by defendant's conduct.

Note: After a court finds a waiver of a predispute arbitration agreement, many defendants overtly delay trial by filing an appeal. To combat this delay tactic, the Consumer Attorneys of California is working with the legislature to pass SB 365. The new bill will allow the case to proceed to trial during the appellate process.

Attorney Michael S. Fields is an experienced mediator and arbitrator with over three decades of experience. He has authored Advocate articles since 1992, and he is again the editor of the Advocate ADR issue. He was CAALA's 2003 president and the recipient of CAALA's prestigious Ted Horn Memorial Award for his contributions to CAALA and the legal profession. He retired from his 47-year personal injury trial practice in 2015. Mr. Fields can be retained as a mediator, arbitrator, referee, or temporary judge by contacting him at msflb@aol.com. His website is www.michaelsfieldslaw.net.

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
July 2023