Supreme Court Number S232946

SUPREME COURT
FILED

DEC 14 2016

Jorge Navarrete Clerk

Deputy

IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT, DIVISION FOUR

SHEPPARD, MULLIN, RICHTER & HAMPTON LLP,

Plaintiff and Respondent,

vs.

J-M MANUFACTURING CO. INC.,

Defendant and Appellant.

Review of the Opinion of the Court of Appeal of the State of California,
(No. B256314)
Los Angeles County Superior Court, Case No. YC067332

APPLICATION OF THE ASSOCIATION OF DISCIPLINE DEFENSE COUNSEL FOR LEAVE TO FILE AN AMICUS CURIAE BRIEF; PROPOSED AMICUS CURIAE BRIEF

Samuel Bellicini
(SBN 152191)
President, Association of
Disciplinary Defense Counsel
Samuel C. Bellicini, Lawyer
1005 Northgate Dr., # 240
San Rafael, CA 94903
(415) 298-7284
Fax: (628) 888-0704

Jerome Fishkin
(SBN 47798)
Fishkin & Slatter LLP
1575 Treat Blvd., Ste 215
Walnut Creek, CA 94598
(925) 944-5600
Fax: (925) 944-5432

Merri A. Baldwin
(SBN 141957)
Rogers Joseph O'Donnell
311 California St., 10th Fl.
San Francisco, CA 94104
(415) 956-2828
Fax: (415) 956-6457

Attorneys for THE ASSOCIATION OF DISCIPLINE DEFENSE COUNSEL
Amicus Curiae on Behalf of Plaintiff and Respondent,
SHEPPARD, MULLIN, RICHTER & HAMPTON LLP.

Supreme Court Number S232946

IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT, DIVISION FOUR

SHEPPARD, MULLIN, RICHTER & HAMPTON LLP,

Plaintiff and Respondent,

vs.

J-M MANUFACTURING CO. INC.,

Defendant and Appellant.

Review of the Opinion of the Court of Appeal of the State of California,
(No. B256314)
Los Angeles County Superior Court, Case No. YC067332

APPLICATION OF THE ASSOCIATION OF DISCIPLINE DEFENSE COUNSEL FOR LEAVE TO FILE AN AMICUS CURIAE BRIEF; PROPOSED AMICUS CURIAE BRIEF

Samuel Bellicini
(SBN 152191)
President, Association of
Disciplinary Defense Counsel
Samuel C. Bellicini, Lawyer
1005 Northgate Dr., # 240
San Rafael, CA 94903
(415) 298-7284
Fax: (628) 888-0704

Jerome Fishkin
(SBN 47798)
Fishkin & Slatter LLP
1575 Treat Blvd., Ste 215
Walnut Creek, CA 94598
(925) 944-5600
Fax: (925) 944-5432

Merri A. Baldwin
(SBN 141957)
Rogers Joseph O'Donnell
311 California St., 10th Fl.
San Francisco, CA 94104
(415) 956-2828
Fax: (415) 956-6457

Attorneys for THE ASSOCIATION OF DISCIPLINE DEFENSE COUNSEL
Amicus Curiae on Behalf of Plaintiff and Respondent,
SHEPPARD, MULLIN, RICHTER & HAMPTON LLP.

TABLE OF CONTENTS

Page(s)

TABLE OF CONTENTS
(Continued)

Page(s)

TABLE OF AUTHORITIES

Page(s)

Federal Cases

California Cases

TABLE OF AUTHORITIES
(Continued)

Page(s)

TABLE OF AUTHORITIES
(Continued)

Page(s)

TABLE OF AUTHORITIES
(Continued)

Page(s)

California Statutes

Other Authorities

APPLICATION FOR LEAVE TO FILE AMICUS CURIAE BRIEF

The Association of Discipline Defense Counsel (ADDC) requests leave to file an *amicus curiae* brief in this matter in accord with Rule 8.520(f) of the California Rules of Court. This amicus brief supports the outcome sought by petitioner Sheppard Mullin, though not for the same reasons.

ADDC is an unincorporated association of attorneys who specialize in representing other attorneys in State Bar disciplinary and admissions matters. Most of our members also represent and advise clients about professional responsibility matters, from conflicts of interest to trust accounts to attorney client fee agreements. Most of our members represent clients in attorney client fee disputes, legal malpractice cases, and matters concerning the admission of law students to practice law. Many of our members are also experienced expert witnesses in matters involving attorney professional responsibility. ADDC has previously appeared as amicus before this court in the *quantum meruit* case of *Huskinson & Brown LLP v. Wolf* (2004) 32 Cal. 4th 453. In that case, ADDC argued the *quantum meruit* position.

ADDC members have special expertise in the issues before this court. Our members are attorneys who regularly advise attorneys and law firms about conflicts of interest, conflict consents and waivers, and attorney fees. Our members regularly draft those conflict consents for themselves and for their clients. Our members also frequently advise attorneys about the issues of disgorgement, entitlement to fees and the determination of reasonable fees or *quantum meruit*.

We believe that there are relevant cases and other authorities relevant to the issues in this matter that have not been cited by either of the parties. We cite and discuss them in our proposed brief. We also propose to this Court standards that we request this Court set forth to determine whether and in what circumstances disgorgement and fee forfeiture may be appropriate, and when attorneys are otherwise entitled to fees, whether contractual fees or reasonable fees as determined by a court.

DISCLOSURE OF AUTHORSHIP OR MONETARY CONTRIBUTION

No party or counsel for any party authored any portion of this brief. No party or counsel for any party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than the *amicus curiae* made a monetary contribution intended to fund the preparation or submission of this brief.

Dated: December 1, 2016 Respectfully submitted,

ROGERS JOSEPH O'DONNELL, PC

By: _____
MERRI A. BALDWIN

Samuel C. Bellicini
SAMUEL C. BELLICINI, LAWYER

Jerome Fishkin
FISHKIN & SLATTER LLP

Attorneys for The Association of Discipline Defense Counsel

AMICUS CURIAE BRIEF

INTRODUCTION

The Association of Disciplinary Defense Counsel ("ADDC") submit this amicus brief on two of the three issues identified in the Court's briefing order of March 9, 2016: whether a sophisticated consumer of legal services can give its informed consent to an advance waiver of conflicts; and whether a conflict of interest that causes no damage to the client and did not affect the value or quality of the attorney's work nonetheless automatically requires the attorney to disgorge all legal fees and preclude the attorney from receiving the reasonable value of the unpaid work.

Based on its members' experience advising and defending attorneys in civil as well as disciplinary matters, the ADDC requests this Court to set forth a standard concerning the enforceability of advance waivers that includes consideration of the relative sophistication of the client who agreed to the waiver, including whether it had the advice of independent counsel, as part of the determination of informed consent. Such a standard would be consistent with California law concerning the enforceability of attorney-client fee agreements, and would allow clients greater choice and flexibility in choosing counsel, in part because by giving lawyers a greater certainty that client waivers will likely be enforced, the universe of attorneys available to clients will expand.

On the issue of the disgorgement of fees, the ADDC requests this Court decline to adopt a rule of automatic disgorgement of fees in all situations involving an attorney's conflict of interest, but instead adopt a standard for determining reasonable attorney's fees

that includes consideration of the value of the services provided because a rule of automatic disgorgement is contrary to established California law and risks creating a disincentive for lawyers to represent multiple parties, as well as increasing the risk of fee disputes among lawyers and clients.

I. A SOPHISTICATED CONSUMER OF LEGAL SERVICES, REPRESENTED BY COUNSEL, CAN GIVE ITS INFORMED CONSENT TO AN ADVANCE WAIVER OF CONFLICTS OF INTEREST WHERE SUCH A CLIENT IS IN A SUFFICIENTLY EQUAL BARGAINING POSITION WITH THE ATTORNEY TO CONCLUDE THAT THE CLIENT FAIRLY CONSENTED TO THE WAIVER.

While this Court has not yet had the opportunity to determine whether a sophisticated client who is represented by counsel can give informed consent to an advance waiver of a conflict of interest, California law has enforced attorney fee agreements against sophisticated clients who were represented by counsel in negotiating those agreements. These cases, while applying a different rule of professional conduct than is at issue here, are instructive because they recognize the principle that certain clients are likely to be in a position of equal bargaining power with the law firms that represent them, and thus the agreements those clients make with their chosen counsel should be enforced. The sophistication of a client is but one factor that merits consideration by a court when determining the enforceability of a consent and waiver of conflicts, just as it is when a court determines the enforceability of an attorney-client fee agreement. Enforcing such agreements allows both attorneys and clients greater certainty in entering into attorney-client representation

agreements, which in turn gives clients greater flexibility and choice of counsel.

A. California Courts Have Considered and Relied Upon the Sophistication of Clients in Enforcing Fee Agreements Between Lawyers and Clients.

A client's level of sophistication is a familiar consideration courts weigh when determining the enforceability of attorney-client fee agreements under the unconscionability rule of Rule of Professional Conduct 4-200. "Unconscionability" for purposes of Rule of Professional Conduct 4-200(b), and general contract law, depends on factors similar to those raised in briefing of this case: equal bargaining power in the form of client sophistication and representation by counsel (procedural unconscionability) versus the harshness or one-sidedness of the agreement (substantive unconscionability).

> [A] contract is largely an allocation of risks between the parties, and therefore [ ] a contractual term is substantively suspect if it reallocates the risks of the bargain in an objectively unreasonable or unexpected manner. [Citations.] But not all unreasonable risk allocations are unconscionable; rather enforceability of the clause is tied to the procedural aspects of unconscionability . . . such that the greater the unfair surprise or inequality of bargaining power, the less unreasonable the risk allocation which will be tolerated.

Cotchett, Pitre & McCarthy v. Universal Paragon Corp. (2010) 187 Cal. App. 4th 1405, 1419-20 [internal citations omitted].

On facts that raise certain issues similar to those raised in this case, the Court of Appeal in *Cotchett* refused to permit a client, Universal Paragon Corp. (UPC), to avoid its fee agreement with the Cotchett law firm, in large part because it found that UPC was a sophisticated client who was represented by counsel at the time the fee agreement was executed. *Cotchett* was decided under Rule of Professional Conduct 4-200(b), which provides, among other enumerated factors for determining the conscionability of a fee, the "relative sophistication of the member and the client." Rule 4-200(b)(2).

In *Cotchett*, the client, UPC, was a property developer who wanted to sue Ingersoll-Rand in order to take control over contaminated property owned by Ingersoll-Rand, which abutted UPC's property. UPC wanted to control the environmental clean-up of the polluted Ingersoll-Rand property, and then develop both properties for a new project. 187 Cal. App. 4th at 1409. UPC hired separate outside counsel to negotiate a fee agreement with the Cotchett firm. The final fee agreement provided for a hybrid contingency/hourly fee agreement whereby Cotchett would be entitled to a contingency fee that was to be based on the total monetary recovery and competing valuations of any real property UPC might be awarded, which would operate as a partial credit against Cotchett's hourly fee. *Id.* at 1410-12.

Cotchett successfully settled the UPC/Ingersoll-Rand case, and almost immediately, UPC balked at paying the firm the

agreed-upon fee. The parties attended non-binding fee arbitration under the Mandatory Fee Arbitration Act (Bus. & Prof Code sections 6200, et seq.), and then attended private JAMS arbitration. UPC then contended that the Cotchett fee agreement was unconscionable. *Id.* at 1414.

As noted in the Court of Appeal opinion, the JAMS arbitrator specifically rejected UPC's argument that the contingency fee agreement was unconscionable.

> She noted that there had been no disparity in bargaining power between UPC and CP & M; that UPC was a very sophisticated client represented by independent counsel in the negotiation of the fee arrangement; that UPC and its attorney had the opportunity to review the retainer agreement before it was signed; and that CP & M had done an excellent job for UPC, reaching what Hanson had characterized as a "stupendous" result. Contingency fees, in Judge Westerfeld's experience, typically range from 33 percent to 40 percent of a settlement amount, and a contingency of 50 percent is not unconscionable.

187 Cal. App. 4th at 1415.

The Court of Appeal agreed, and held that UPC negotiated the *Cotchett* fee agreement on a level bargaining field, again emphasizing that UPC's level of sophistication and representation by counsel were determinative of this issue.

> On the issue of procedural unconscionability, UPC is a sophisticated corporate client that initiated the Ingersoll–

> Rand litigation to acquire real property it intended to develop as part of a larger project. It employed outside counsel to negotiate the fee agreement with CP & M, and wielded equal bargaining power during those negotiations. The fee agreement was not a contract of adhesion; if UPC had not been satisfied with its terms, it could have employed any of a number of law firms in lieu of CP & M. This was a private business transaction between equally matched parties, pure and simple. (*Ramirez v. Sturdevant* (1994) 21 Cal. App. 4th 904, 913, 26 Cal.Rptr.2d 554 [negotiation of fee agreement is, in general, an arm's length transaction].)

Cotchett, 187 Cal. App. 4th at 1420-21.

Similarly, in *Desert Outdoor Advertising v. Superior Court* (2011) 196 Cal. App. 4th 866, the Court of Appeal enforced an arbitration clause in an attorney-client fee agreement against clients who "were the president of a corporation well-known for its prominence in the billboard industry, as well as another businessman." *Id.* at 874. The *Desert Outdoor* Court correctly recited that, "[t]he scope of a fiduciary's obligations depends on the specific facts of the case. Such factors may include, for example, the relative sophistication and experience of the vulnerable party." *Id.* at 873 (citations and internal notations omitted).

In *Ferguson v. Yaspan* (2014) 233 Cal. App. 4th 676, the attorney Yaspan entered into a business agreement with his client Ferguson, to purchase fifty percent of a trust Ferguson owned. Yaspan did not comply with the written consent requirement of Rule

of Professional Conduct 3-300. Nevertheless, in a lawsuit brought by Ferguson's heir to avoid the agreement, the Court of Appeal enforced the agreement in part because Ferguson had hired independent counsel to review the draft agreement with Yaspan. 233 Cal. App. 4th at 687-89.

In all of these cases, the Court found that the sophistication of the client, and particularly the involvement of outside independent counsel in the negotiation of the agreement at issue, to be determinative in establishing the fairness and validity of the fee agreement. The courts expressly recognized that client sophistication materially affected the relative position of the client versus the lawyer in the negotiation process of the parties' representation agreement. With the involvement of outside independent counsel on behalf of the client in the negotiation process, any perceived advantage or superior position the contracting lawyer might otherwise have had was substantially mitigated, resulting in both parties having equal bargaining power.

B. A Client's Sophistication is One Factor That Should Weigh in Favor of Enforcing an Advance Waiver

For similar reasons as those that underlie preceding courts' determinations of the enforceability of fee agreements, courts should weigh a client's sophistication when considering the enforceability of advance waivers, particularly the participation of separate counsel. Where clients are experienced and sophisticated legal consumers, represented by separate counsel, and those clients understand the meaning of a conflict waiver, those factors should

weigh in favor of finding the waiver valid and enforceable. Moreover, important policy reasons exist to support the enforcement of advance waivers circumstances such as this, including fostering the goal of promoting greater certainty and reliability of such waivers and allowing larger law firms to take on the representation of a greater range of clients, thereby fostering an expanded choice of counsel for sophisticated clients who often demand a wide range of counsel to assist on a wide range different matters. Therefore, courts should weigh the relative sophistication of clients when determining whether a particular client's consent was informed under Rule 3-310.

A client's informed consent is required in order for an attorney to undertake any representation that may potentially or actually conflict with the interests of other clients of that attorney. Rule 3-310(C). Accordingly, without informed consent, a law firm may not accept clients whose interests might conflict with other clients, even if on unrelated matters. For large law firms, with a diverse and extensive book of clients involved in different industries and sectors, such potential and actual conflicts would effectively limit the diversity of clients they represent unless each of those clients consents to the conflicts that exist and may exist. In turn, certain large corporate clients who need or require employment of a number of law firms recognize that they need to agree to advance waivers in order to retain certain of the law firms they want to represent them, and, as was the case here, routinely provide such consents. *See, e.g., Galderma Laboratories, L.P. v. Actavis Mid-Atlantic LLC* (2013) 927 F.Supp. 2d 390, 406.

Rule 3-310 states that "informed written consent" means "the client's or former client's written agreement to the representation following written disclosure." Rule 3-310(A)(2). "Disclosure" means "informing the client or former client of the relevant circumstances and of the actual or reasonably foreseeable adverse consequences to the client or former client." Rule 3-310(A)(1). The purpose of the rule, then, is to ensure that a client's consent is informed by the client's awareness of what the client is actually agreeing to by providing such consent.

In this context, there is no sound reason not to consider a client's level of sophistication among the factors to be considered when weighing the validity and enforceability of the consent, and in particular whether it was represented by independent counsel in connection with the waiver. A corporate client, represented by counsel, experienced in litigation and familiar with conflict waivers and the rules governing conflicts, should be held to a higher level of understanding of the contents of such agreements than other clients should be. "When a client has their own lawyer who reviews the wavier, the client does not need the same type of explanation from the lawyer seeking a waiver because the client's own lawyer can review what the language of the waiver plainly says and advise the client accordingly." *Galderma Laboratories L.P.*, 927 F. Supp. 2d at 405. The California State Bar recognized this in its Formal Ethics Opinion 1989-115, when it stated that "it is possible in appropriate circumstances and with knowledgeable and sophisticated clients to clarify obligations and responsibilities by agreements of [advance waivers]." Cal. Formal Opin. 1989-115.

Lawyers must necessarily rely upon the validity and enforceability of waivers in taking on clients whose interests may conflict with other clients of the lawyer or law firm. Clients, too, have an interest in seeing these agreements enforced, since that predictability ensures the availability of the largest number of potential lawyers and law firms available for representation in a given matter. When facts demonstrate that a sophisticated client knowingly entered into a conflict waiver, freely provided consent, and understood the terms and meaning of that consent, there are significant reasons to find such a consent valid and enforceable, and that determination is entirely consistent with Rule 3-310.

In the present case, the Court of Appeal did not consider the relative sophistication of the client, J-M Manufacturing Co. ("J-M"), in finding that the conflict waiver was unenforceable. Rather, the court's analysis focused almost entirely on the fact that Sheppard Mullin had not specifically disclosed the "potential or actual conflict" with South Lake Tahoe, and did not obtain J-M's informed written consent to continued representation once the law firm began advising South Lake Tahoe after the J-M representation began. 244 Cal. App. 4th at 613.

However, by omitting consideration of the relative sophistication of the client, and the fact of involvement of the client's in-house counsel, the Court of Appeal's analysis elevates one factor – the specific identification of South Lake Tahoe as a client or former client of the firm's with interests that conflict with J-M's interests – over all other factors that are undeniably relevant to a determination of whether the client's consent was informed. This approach thus

imposes on Rule 3-310 a bright-line test that is not present in the rule itself. The terms of the waiver that J-M signed specifically provided, in part, that "We may currently or in the future represent one or more other clients (including current, former and future clients) in matters involving [J-M]." 244 Cal. App. 4th at 599. (Emphasis omitted.) The waiver goes on to specify that, pursuant to this waiver, the law firm:

> . . . may represent another client in a matter in which we do not represent [J-M], even if the interests of the other client are adverse to [J-M] (including appearance on behalf of another client adverse to [J-M] in litigation or arbitration) and can also, if necessary, cross-examine [J-M] personnel on behalf of the other client in such proceedings . . . provided the other matter is not substantially related to our representation of [J-M] and in the course of representing [J-M] we have not obtained confidential information of [J-M] material to representation of the other client.

244 Cal. App. 4th at 599. (Emphasis omitted.)

Thus, the plain language of the waiver that J-M negotiated through its separate counsel and signed, specifically included an express agreement by the client that Sheppard Mullin could not only represent other clients whose interests are adverse to J-M's in the *qui tam* matter, but also clients in a far more directly adverse circumstance: representing clients in litigation against J-M. In consenting to that potential conflict, arguably a far more significant and directly adverse conflict than was present here, J-M was represented by experienced in-house counsel; had the opportunity to and did negotiate the agreement with the law firm (although apparently raised no questions concerning the waiver) and agreed to

the terms of this waiver.[1] In that context, it is hard to understand why Sheppard Mullin's failure to specifically disclose its South Lake Tahoe representation created grounds upon which to void the waiver. The Court of Appeal did not explain why the failure to disclose the prior representation of South Lake Tahoe either at the time the representation began or later was such a material fact that it rendered J-M's consent invalid. When J-M's experience, sophistication and representation by independent counsel is considered, the fact that the law firm failed to specifically disclose that South Lake Tahoe had been or was a client for purposes of an unrelated employment advice matter does not, by itself, provide an obvious basis upon which to conclude that J-M did not understand what it was waiving when it provided the consent at issue.

California law recognizes the general principle that a representation agreement between a lawyer and a client is a contract that must be enforced by its terms, in accordance with the plain meaning of those terms. *M'Guinness v. Johnson* (2015) 243 Cal. App. 4th 602, 617. By failing to consider the sophistication of the client and particularly the participation of independent counsel in connection with a conflict consent and waiver, the Court of Appeal improperly tilted the balance between client and lawyer, and created a situation in which the only relevant factor is whether or not specific

[1] The Court in *Galderma Laboratories L.P.* noted that in-house counsel, while employed by the company, "is still [a] lawyer *independent* from [the law firm], advising Galderma on whether or not Galderma should give its consent." 927 F. Supp. 2d at 403. *See also* Restatement (Third) of Law Governing Lawyers, §122, comment c(i) (2000).

conflicts were disclosed. In light of the specific terms of the waiver J-M knowingly agreed to, applying that bright-line test unfairly penalizes the law firm, particularly where a sophisticated client accepted the specific risks plainly set forth in that waiver.

II. A CONFLICT OF INTEREST THAT UNDISPUTEDLY CAUSED NO DAMAGE TO THE CLIENT AND DID NOT AFFECT THE VALUE OR QUALITY OF AN ATTORNEY'S WORK SHOULD NOT AUTOMATICALLY (I) REQUIRE THE ATTORNEY TO DISGORGE ALL PREVIOUSLY PAID FEES, AND (II) PRECLUDE THE ATTORNEY FROM RECOVERING THE REASONABLE VALUE OF THE UNPAID WORK

Under present law established by this Court, the existence of a conflict of interest or any other attorney breach of duty does not provide grounds for automatic disgorgement of previously paid fees. Rather, each case is considered separately, on its facts. There is no policy reason to change that principle. The body of case law that concerns the determination of attorney fees by analyzing the reasonable value of that work, the *quantum meruit test*, includes standards that allow a court to evaluate and possibly decrease fees as a result of an attorney's conflict of interest or breach of any other attorney duty.

Rather than establish a rule that would create a risk of inconsistent (and unfair) application through an automatic disgorgement standard, this Court should instead establish standards for disgorgement that are similar to the standards used in determining reasonable value of fees.

The standards that are most consistent with current case law and principle of fairness would be (1) each case has to be