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California Supreme Court Provides Clarity As To How Costs Are To Be Recovered In Arbitration Based On A Statutory Offer To Compromise, And A Warning To Counsel...

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As many are aware, Code of Civil Procedure section 998 creates an incentive for settlement. It authorizes an award of costs to a party that makes a pretrial settlement offer when the opponent rejects the offer and obtains a lesser result at trial. See, Martinez v. Brownco. Construction (2013) 56 Cal.4th 1014. In 1997, the California legislature amended the Offer to Compromise statute to make the same incentive available in arbitrations. However, the revised statute is not explicit as to the forum in which costs are to be obtained in arbitration.

Significant guidance has been provided as to that issue in the case of Heimlich v. Shivji (2019) Westlaw 2292828 ("Heimlich"). In an opinion published May 30, 2019 by the California Supreme Court, the Court ruled that a Request for Costs under Code of Civil Procedure section 998 is timely if filed with the arbitrator within 15 days of final award. The California Supreme Court further held that, in response to a Request for Costs, an arbitrator has the authority to award costs to the offering party, so long as it is made within the 15 days called for the filing of a Memorandum of Costs (post trial). However, the Court further held that if an arbitrator refuses to award costs, based on the arbitrator's mistaken belief that the arbitrator does not have jurisdiction following the issuance of the award, costs will be *forfeited* by the prevailing party as the trial court does not have the discretion to award costs (it can only affirm the award).

The holding in Heimlich makes it clear that a party which has issued an Offer to Compromise prior to the arbitration should obtain a Stipulation that the Offer can be put into evidence at the arbitration for the sole purposes of assuring that the arbitrator is aware of the Offer and that a request for costs will be issued within 15 days of the award and that the arbitrator will retain jurisdiction to rule on an award of costs.

The facts of the Heimlich case are relatively routine. In 2003, an engineer and inventor, Shiraz Shivji, retained attorney Alan Heimlich to handle a range of intellectual property matters. The representation agreement included a clause providing for arbitration of disputes. In 2012, Heimlich sued Shivji alleging that Heimlich was owed roughly \$125,000 in legal fees. After a year into the litigation, Shivji made an offer to settle the case under Code of Civil Procedure section 998 for \$30,001. The offer was not accepted.

Thereafter, Shivji filed a Demand for Arbitration with the American Arbitration Association. The trial court later granted Shivji's Motion to Compel Arbitration and stayed further litigation. The litigation was quite contentious. Shivji and Heimlich filed claims against each other with Shivji asking for a refund of \$176,000 for sums already paid, and with Heimlich seeking \$125,000 for unpaid legal fees. Each party also requested costs.

In March 2015, the arbitrator issued an award granting \$0 to both Heimlich and Shivji and directed that each party will bear their own attorney's fees and costs. Six days after the issuance of the award, Shivji advised the arbitrator of the original section 998 Offer and a second one for \$65,001. Shivji argued for costs, asserting that Heimlich had failed to obtain a more favorable result. The arbitrator replied by email stating that he had no further jurisdiction. Shivji then went to the trial court to confirm the arbitration award and attached a Memorandum of Costs seeking \$76,684.02. The trial court confirmed the award but refused to add costs. The trial court relied on Maaso v. Signer (2012) 203 Cal.App.4th 362, which held that a request for section 998 costs in connection with an arbitration must be resolved by the arbitrator.

On appeal, the Court of Appeal reversed, holding that Shivji's post-award request to the Arbitrator was timely. The Court of Appeal further ruled that the trial court could vacate the arbitrator's award because the arbitrator had refused to hear the evidence as to costs (a victory for Shivji).

The matter then came before the California Supreme Court. The California Supreme Court ruled that the allocation of costs was an issue for the arbitrator in the first instance. The California Supreme Court further ruled that evidence of a section 998 Offer may be presented before or after a final arbitration award, so long as the request for costs occurs within 15 days of the issuance of the final award. The Supreme Court noted that the Shivji Offer could have been presented, on a limited basis, before the award, but that was not required. The Court went on to rule, and rejected, Heimlich's assertion that allowing a section 998 Offer to be raised after a final award would destroy the finality of arbitration awards.

However, the California Supreme Court also held that the conclusion that Shivji's request was timely does not automatically entitle him to judicial relief. The Court noted that the court's power to correct or vacate an erroneous arbitration award is closely circumscribed. The Court further noted that most legal errors in arbitration are not reviewable. The Court noted the arbitrator refused to consider Shivji's request for costs, and that on its face, the arbitrator's response shows the arbitrator believed he lacked jurisdiction to consider Shivji's request, which was in error. The Court went on to rule that, while the arbitrator's conclusion was incorrect, ordinary errors in ruling on costs are not subject to correction by the trial court, nor do they serve as a basis for vacating an award. The Court went on to hold that, as the party challenging the arbitrator's award and the trial court's judgment, it was Shivji that had to establish his entitlement to relief. The Court noted that Shivji did not seek a stipulation that would allow the parties jointly to advise the arbitrator of a section 998 Offer, and that Shivji chose to wait until shortly

after the arbitrator's merits award to raise the issue. While Shivji was legally entitled to do so, the Court ruled that Shivji ran the risk that the arbitrator would erroneously refuse to award costs, leaving him without recourse under the narrow grounds for vacation of or correction contained in the statutory scheme for arbitration. Shivji then lost on his appeal to obtain costs and was awarded no costs.

The California Supreme Court has now spoken on this important issue. If there is section 998 Offer before arbitration, the offering party should alert the arbitrator in advance of the arbitral hearing to ensure that the arbitrator is aware of the Offer and an agreement is worked out as to the arbitrator ruling on costs.

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