2d Civil Nos. B261860, consolidated with B264964

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION ONE

WILLIAM E. RICE, et al.

Plaintiff, Respondent, and Cross-Appellant,

vs.

GARY P. DOWNS,

Defendant, Appellant, and Cross-Respondent.

Appeal from Los Angeles Superior Court, Central District
Los Angeles Superior Court Case No. BC506921
Honorable Yvette M. Palazuelos

COMBINED RESPONDENT'S BRIEF AND APPELLANT'S OPENING BRIEF

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TO BE FILED IN THE COURT OF APPEAL **APP-008**

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APPELLANT/PETITIONER: WILLIAM E. RICE, et al. RESPONDENT/REAL PARTY IN INTEREST: GARY P. DOWNS	
CERTIFICATE OF INTERESTED ENTITIES OR PERSONS (Check one): ☑ INITIAL CERTIFICATE ☐ SUPPLEMENTAL CERTIFICATE	

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1. This form is being submitted on behalf of the following party (*name*): Respondent and Cross-Appellant William E. Rice

2. a. ☐ There are no interested entities or persons that must be listed in this certificate under rule 8.208.

   b. ☑ Interested entities or persons required to be listed under rule 8.208 are as follows:

Full name of interested entity or person	Nature of interest (Explain):
(1) Highland Property Development	Plaintiff
(2) Highland Property Construction, Inc	Plaintiff
(3) Douglas Day	Plaintiff and Member/Shareholder of 1 and 2 above
(4) Kristoffer Kaufmann	Member/Shareholder of 1 and 2 above
(5) Nixon Peabody LLP	Defendant

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The undersigned certifies that the above-listed persons or entities (corporations, partnerships, firms, or any other association, but not including government entities or their agencies) have either (1) an ownership interest of 10 percent or more in the party if it is an entity; or (2) a financial or other interest in the outcome of the proceeding that the justices should consider in determining whether to disqualify themselves, as defined in rule 8.208(e)(2).

Date: September 2, 2015

Jeffrey E. Raskin ▶ _____

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INTRODUCTION

For over two years, William Rice has been seeking the basic opportunity to present the merits of his claim that his attorney and business partner, Gary Downs, breached his fiduciary duties. To this day, those claims have never seen the light of a courtroom or an arbitration hearing.

Rice lost his opportunity for a superior court trial when the court erroneously ordered his claims into arbitration. There were two distinct errors:

First, Rice's tort claims are well outside of the scope of the arbitration clause in the business' operating agreement. The case law firmly establishes Rice's narrow interpretation, and the contract's express language nails the door closed. In a consent-to-jurisdiction clause, the parties agreed that all of the claims "arising out of, under or in connection with this Agreement or the transactions contemplated by this Agreement" would be subject to the jurisdiction in California. In the very next paragraph, they agreed to arbitrate only a subset of those claims—claims "arising out of" the agreement. They thus, *excluded* the "in connection with" language that courts had regularly held encompassed tort claims.

Second, even if all of the claims against Downs were arbitrable, the trial court failed to exercise its statutory discretion to deny or stay arbitration given the undeniable and conceded overlap and risk of inconsistent results between (a) the arbitration of the fiduciary duty claims against Downs and (b) the litigation of those identical fiduciary claims

against Downs' law firm, Nixon Peabody, which was not subject to the arbitration agreement. Indeed, Nixon Peabody actually urged the court to deny arbitration of those overlapping claims. But the trial court erroneously thought there was no statutory basis to do so, having considered and rejected the potential overlap between a *different* set of claims concerning whether Downs and Nixon Peabody were entitled to charge for Downs' legal services to the parties' company.

Rice lost even the opportunity to arbitrate his claims when Downs and Nixon Peabody engaged in what the trial court called a "coordinated campaign" to delay and deny Rice's ability to prosecute his claims in arbitration: A systematic denial of discovery in which Downs claimed that he couldn't provide documents—even his own emails—because they belonged to Nixon Peabody, where he was then a partner. Nixon Peabody avoided production by going so far as to use building security to bar a process server from serving a subpoena. In the face of an impending arbitration hearing, Rice dismissed his claims without prejudice. Downs then convinced the arbitrator to convert that dismissal into a dismissal with prejudice. The trial court recognized the injustice and vacated the award based on the court's inherent powers rather than a statutory ground for vacatur. But the statute provides a ground for what happened here: When one party uses procedural maneuvers to deny the other a fair opportunity to present his case on the merits, the resulting award must be vacated because it was obtained by "undue means."

The Court should reverse the order compelling arbitration, which necessarily negates the arbitration and moots the trial court's later order regarding the award. But at very least, the Court should affirm the trial court's decision to vacate the award to the extent that the arbitrator dismissed Rice's claims with prejudice. Either way, it is time for Rice to finally have an opportunity to present his case.

STATEMENT OF FACTS

As parties must, we state the facts favorably to the trial court's decision to vacate the arbitration award. As to arbitrability, the governing facts are the undisputed terms of the arbitration agreement and the nature of (but not the truth of) the complaint's allegations.

A. The Parties And Their Shared Business.

Gary Downs is an attorney who William Rice alleges entered into business transactions with his clients: Rice, Douglas Day and Kristoffer Kaufmann. (16 AA 4408; see also e.g., 6 AA 1441-1445, 1513-1517.) Downs was a partner at Pillsbury Winthrop LLP and then at Nixon Peabody LLC. (1 RA 41-42 at ¶¶ 2, 4.)

Rice, Downs and Kaufmann formed Highland Property Development, LLC (HPD) and related companies to develop affordable housing projects. (1 RA 42 at ¶ 3; 2 AA 399; 6 AA 1513, 1517.) In 2007, they admitted Day as a member of HPD, memorialized by an amended and restated operating agreement. (1 RA 42 at ¶ 5, 85-114; 2 AA 399-400; 6 AA 1441-1442.) Both the original and amended operating agreements

were prepared by Pillsbury, where Downs was then a partner. (3 RA 540-542 at ¶¶ 2-5; 6 AA 1441 at ¶ 7.)

Throughout the proceedings, Downs consistently testified that Rice and Day were never his or his firms' clients—that the firms represented HPD and never the individuals. (See pp. 28-29, *post.*)

Documents prepared by Downs' firms tell a different story: Twenty-three formal opinion letters authored by the firms and submitted to financial institutions and federal agencies state unequivocally that the firms were acting as counsel to the individual members of the business, specifically including Rice and Day. (See pp. 29-30, *post*.)

B. The Arbitration Agreement.

The original and amended operating agreements each contain two key provisions addressing claims among the parties:

- In the consent-to-jurisdiction clauses, the parties consented to jurisdiction in California courts in any action on a claim "arising out of, under or in connection with this Agreement or the transactions contemplated by this Agreement." (1 RA 74 at ¶ 12.4 [original agreement], 110 at ¶ 13.4 [amended agreement].)

- In the arbitration clause, which is the very next paragraph in both agreements, the parties agreed to arbitrate only claims "arising out of this Agreement." (1 RA 74 at ¶ 12.5 [original agreement], 110 at ¶ 13.5 [amended agreement].)

The arbitration clause also provides that "[t]he arbitrator shall not have any power to alter, amend, modify or change any of the terms of this Agreement nor to grant any remedy which is either prohibited by the terms of this Agreement, or not available in a court of law." (1 RA 74-75 at ¶ 12.5, 110-111 at ¶13.5.)

C. Kaufmann Commences An Arbitration.

Allegedly at Downs' urging, Downs, Rice and Day removed Kaufmann as an HPD member and manager. (1 RA 7.) Kaufmann demanded arbitration to resolve whether his removal violated the parties' agreements. (2 RA 406, 445-447.)

D. Rice And Day Sue Downs And Nixon Peabody For Breach Of Fiduciary Duty.

Rice and Day later filed a lawsuit against Downs and Nixon Peabody, alleging, among other things, multiple breaches of fiduciary duty. (1 RA 4-18.) Downs' own counsel later underscored the magnitude of these claims, calling them "enormous." (7 AA 1811:8-9.)

Malpractice. The complaint alleges that Downs committed malpractice by (1) drafting the operating agreements in a manner that was detrimental to his clients, including Rice and Day; (2) providing poor legal advice on various issues; and (3) failing to advise his clients of potential and actual conflicts and entering into business with clients in violation of rule 3-300 of the California Rules of Professional Conduct (Rule 3-300). (1 RA 9-12.)

Breach of fiduciary duty. The complaint alleges that Downs and Nixon Peabody committed multiple breaches of their fiduciary duty. (1 RA 12-14.) It squarely premises Nixon Peabody's liability on Downs' conduct. Downs allegedly took these actions both "individually and acting as a partner of the law firm Nixon Peabody." (*Ibid.*) For instance, the complaint alleges:

1. Downs, individually and through Nixon Peabody, acted as counsel and provided legal services to Rice and Day. (1 RA 6 at ¶ 7.)

2. Both defendants breached their duty when Downs caused the companies to engage in detrimental financial transactions that benefitted both Downs and "other clients of his and of Nixon Peabody." (1 RA 13-14 at ¶ 25.e.)

3. Both breached their duty and violated Rule 3-300 by failing to disclose and obtain waivers of actual and potential conflicts between Downs and the other HPD members. (1 RA 13 at ¶ 25.a-b.)

4. Both are liable for hundreds of thousands of dollars of damages caused by Downs' interference with transactions that Nixon Peabody was handling, including "caus[ing] the attorneys at Nixon Peabody to take actions that were detrimental" to HPD, Rice and Day. (1 RA 13 at ¶ 25.c.)

Claims for fees charged by Downs. The complaint separately alleges that Downs breached the operating agreements by charging HPD for his legal services. (1 RA 14-16.) It also alleges that Nixon Peabody would

be unjustly enriched if it were able to charge for those same services. (1 RA 16-17.)[1]

Rescission. Rice and Day sought rescission of the operating agreements based on Downs' breaches of fiduciary duty and failure to comply with Rule 3-300. (1 RA 17.)

E. Nixon Peabody Cross-Complains For HPD's Unpaid Legal Fees.

Nixon Peabody filed a cross-complaint against HPD for unpaid legal fees. (2 RA 500-504.) HPD advised the court that it intended to defend those claims by arguing that Nixon Peabody could not seek amounts that Downs was contractually foreclosed from seeking. (2 RA 395, 398.)

F. The Trial Court Compels Arbitration Of The Claims Against Downs And Stays The Remainder Of The Action.

1. In his petition to compel arbitration, Downs concedes that the claims against Nixon Peabody are "not independent."

Downs petitioned to compel arbitration of Rice and Day's claims against him. (1 RA 19-40.) His petition made clear that the claims against Nixon Peabody "are not independent but in fact contain overlapping issues": The fiduciary duty claims "are based on services the firm

[1] Although this impermissible-fee claim was alive during the petition to compel arbitration (e.g., 2 RA 394, 398), Rice and Day withdrew it in the late stages of the arbitration (1 AA 215).

provided, through Downs" and those same issues would be decided in arbitration. (1 RA 38-39.)

Noting that Nixon Peabody was not bound by any agreement to arbitrate, Downs acknowledged that there was a "risk of inconsistent results." (*Ibid*.) He argued that the court was required to stay the claims against Nixon Peabody until the "overlapping issues" were resolved in arbitration. (*Ibid.*)

At about the same time, Downs filed a cross-claim in the Kaufmann arbitration, seeking declaratory relief regarding some of the subjects of Rice and Day's complaint, including a declaration that he did not commit malpractice or violate the Rules of Professional Conduct. (2 RA 451, 460-464, 472-475.)

2. Rice and Day argue that their claims are not arbitrable and that the arbitration of Downs' claims should be stayed.

Rice and Day opposed Downs' petition on the basis that their tort claims were not within the scope of the arbitration agreement. (2 RA 398-401.) Alternatively, they argued that the court should exercise its discretion to deny arbitration pursuant to Code of Civil Procedure section 1281.2, subdivision (c) (section 1281.2(c)), because the claims against Downs and the non-arbitrable claims against Nixon Peabody shared extensive common issues of fact and law, creating a possibility of inconsistent rulings in arbitration and litigation. (2 RA 396-398.)

Rice and Day also petitioned the court to stay the Kaufmann arbitration as to Downs' declaratory relief claims that mirrored their civil complaint. (2 RA 366-383.)

3. Nixon Peabody agrees that the court should deny arbitration of the overlapping fiduciary duty claims.

Nixon Peabody filed a partial opposition to Downs' petition to compel arbitration. (2 RA 509-516.) It agreed with Rice and Day that the trial court "should use its discretion afforded by Code of Civil Procedure section 1281.2(c) to deny arbitration as to the first and second causes of action"—the malpractice and fiduciary duty claims. (2 RA 511-515; see 1 RA 9-14 [complaint].) Nixon Peabody stressed that because Downs allegedly committed the conduct both in his individual capacity and as a Nixon Peabody partner, there was a "possibility of conflicting rulings between the arbitration with Downs and litigation with Nixon Peabody" that triggered section 1281.2(c). (2 RA 511.) Nixon Peabody described the conflict as a "distinct possibility." (*Ibid.*)

Accordingly, Nixon Peabody asked the court to grant Downs' motion to compel arbitration "solely as to the third, fourth, and fifth causes of action"—i.e., the claims that Downs breached the operating agreement by receiving compensation for his services to HPD and the claim for rescission. (*Ibid.*; see 1 RA 14-17 [complaint].)

4. The reply papers confirm the claims' interdependence.

Downs' reply. Downs did not retreat from his earlier concession of overlapping issues or of the "possibility"—the statutory standard—of inconsistent rulings. (3 RA 715-718; see pp. 19-20, *ante*.) Instead, he argued that inconsistent results were not "likely" (3 RA 715) because:

- Rice and Day would lose their claims on the merits because Downs supposedly never represented them and never committed any misconduct (3 RA 710-713, 715-717); and
- The arbitration ruling in favor of Downs "would effectively preclude liability of Nixon Peabody on the same claim." (3 RA 717-718.)

Downs did, however, acknowledge that "a ruling against Downs would not be imputed to Nixon Peabody." (3 RA 718.)

Rice and Day's reply. Rice and Day demonstrated that it was improper for Downs to argue the merits in determining whether the claims should be arbitrated. (3 RA 729-730.) They further argued that if there were two separate proceedings, the fiduciary duty issues would need to be relitigated against Nixon Peabody because res judicata and collateral estoppel would not apply. (3 RA 727-728.)

5. The trial court finds no basis to deny or stay arbitration.

The trial court ordered Rice and Day to arbitrate all of their claims against Downs and stayed the civil action—essentially severing and staying Rice and Day's overlapping litigation against Nixon Peabody. (3 RA 748-749.)

The court did not exercise its discretion under section 1281.2(c) despite Rice and Day's request that it do so. The court stated that in its view, the issue to be arbitrated was Down's right to compensation under the operating agreement and that the agreement is "irrelevant" to the Nixon Peabody litigation. (3 RA 746-748.) "Therefore, there is no basis to deny arbitration" because of possible conflicting rulings. (3 RA 747-748.)

6. This Court denies writ relief.

Orders to arbitrate are not immediately appealable. (*State Farm Fire & Casualty v. Hardin* (1989) 211 Cal.App.3d 501, 506.) Rice and Day sought writ review, which this Court denied. (Case No. B251549.)

G. The Arbitration.

1. Downs' campaign to prevent Rice and Day from pursuing their claims.

Once in arbitration, Downs and Nixon Peabody engaged in what the trial court called a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their claims. (16 AA 4420.) The trial court made detailed factual findings in this regard and credited Rice and Day's

"persuasive[]" charting of Downs and Nixon Peabody's "campaign." (*Ibid.*) This is what happened:

Rice and Day made repeated efforts to obtain critical information from Downs, both through informal information exchanges under the arbitration rules and through formal discovery requests. (12 AA 3166 at ¶¶ 3-4; 16 AA 4419-4420.) Although Downs was then a Nixon Peabody partner, he claimed that he could not provide responsive documents in Nixon Peabody's possession, including emails that he himself had sent or received. (12 AA 3166-3167 at ¶¶ 3-5, 3190-3201.) In late September 2013, that was Downs' response to nearly every document request Rice and Day propounded. (12 AA 3190-3201.)

Rice and Day's counsel then asked Nixon Peabody's counsel in the stayed litigation, Kevin Brogan, to accept service of a business records subpoena that covered the same requests propounded to Downs. (12 AA 3167-3168 at ¶ 9, 3206-3219.) Brogan did not immediately respond.

Rice and Day's counsel complained to the arbitrator. (12 AA 3168-3169 at ¶ 12.) Downs' counsel then advised Rice and Day that Nixon Peabody would allow Downs to produce responsive documents provided that they were limited to emails between Downs and Rice, Day or Kaufmann. (12 AA 3168-3169, 3250.) Rice and Day's counsel explained why the proposed limitation was not acceptable: Relevant documents could

easily be addressed between Nixon Peabody attorneys or between Nixon Peabody attorneys and third parties. (12 AA 3169, 3253.)

Brogan still had not responded nearly two weeks after Rice and Day asked whether he would accept service of the subpoena. (12 AA 3169 at ¶ 16.) Rice and Day's counsel then followed up by email and telephone. (12 AA 3169 at ¶ 16, 3261.) Ultimately, Brogan said that he was not authorized to accept service on Nixon Peabody's behalf. (12 AA 3170 at ¶ 19.)

But when Rice and Day attempted to serve the subpoena on Nixon Peabody's Los Angeles office, building security barred the process server from going up to the firm's floor and refused to accept service on Nixon Peabody's behalf. (12 AA 3170 at ¶ 20, 3277.)

At the same time, Downs aggressively pushed for and obtained the completion of all depositions without having produced the documentary evidence that Rice and Day were struggling to obtain. (16 AA 4420; 12 AA 3168-3170.)

The arbitrator ultimately ordered Downs to accept service of Rice and Day's subpoena on Nixon Peabody's behalf. (16 AA 4420; 12 AA 3170, 3282.) The situation was so bad that the arbitrator also ordered that "[i]f for some reason Downs cannot accept service or Downs is prevented by Nixon from accepting service, Downs must arrange to escort a process server through security at Nixon to a person who is authorized to accept service on Nixon's behalf." (12 AA 3282.)

Downs later tried to blame Rice and Day's counsel for not acting diligently in seeking discovery—a characterization that the trial court rejected as "misleading." (16 AA 4419.)

2. Left with no way to prosecute their fiduciary duty claims in the impending arbitration hearing, Rice and Day dismiss their claims without prejudice.

On December 17, 2013, with the arbitration hearing less than a month away (January 13, 2014), Downs and Nixon Peabody had still not produced the responses. (12 AA 3171; 16 AA 4409, 4420-4421.) That not only directly deprived Rice and Day of discovery, it also prevented them from effectively deposing Nixon Peabody attorneys. (12 AA 3171.)

Rice and Day's counsel advised Downs and the arbitrator that they would be forced to withdraw their claims without prejudice "because we have been frustrated in our efforts to obtain emails and other documentation from Mr. Downs and his firm." (12 AA 3171, 3286, 3289-3290; 16 AA 4421.)

Then, on the Friday before Christmas (the following Wednesday), Nixon Peabody mailed a flood of materials—20,000 emails and nearly 34,000 other documents. (7 AA 1875 at ¶ 8; 12 AA 3171; 16 AA 4421.) The trial court found that this production was both unwieldy and incomplete. (16 AA 4421; see 12 AA 3292.)

The following Monday, December 23, Rice and Day formally filed a dismissal of their claims without prejudice. (12 AA 3171, 3294-3295.)

They had not yet received even the incomplete production that Nixon Peabody had mailed, and it was now less than three weeks before the arbitration hearing. (12 AA 3171.)

3. Downs capitalizes on the situation he created by asking the arbitrator to convert the dismissal without prejudice into a dismissal with prejudice.

Having left Rice and Day with no alternative but to dismiss, Downs then asked the arbitrator to convert their dismissal *without* prejudice into a dismissal *with* prejudice pursuant to a rule of the arbitration organization. (2 AA 514-522.) Over Rice and Day's opposition, the arbitrator granted Downs' request. (1 AA 166-168; 16 AA 4409.)

4. The arbitration award.

The final award again noted that Rice and Day's claims had been dismissed with prejudice. (1 AA 156.) It did not decide Downs' declaratory relief claims concerning his alleged legal malpractice and breach of fiduciary duty. Instead, the arbitrator resolved only (a) Kaufmann's claims; (b) Downs' claims for monetary relief; (c) Downs' requests for declaratory relief concerning whether the operating agreement precluded him from billing for legal services and the enforceability of a prior settlement agreement with Kaufmann; and (d) derivative claims asserted by HPD. (1 AA 165, 251-252; see also 1 AA 201-253.)

H. Downs' Statements That His Firms Never Represented Rice Or Day Individually And The Discovery Of Contrary Evidence.

At every stage—from his petition to compel arbitration onward—Downs repeatedly testified that he and his firms never represented Rice and Day individually, and his counsel urged that Rice and Day's claims were therefore meritless. (E.g., 3 RA 750-768.) For instance:

- In his petition to compel arbitration, Downs declared that he and his firms did not represent Rice with respect to the original operating agreement and that after the formation of HPD, "Pillsbury began representing HPD, but not any of its individual Members." (1 RA 42 at ¶ 4.)
- During his pre-arbitration deposition, Downs repeatedly testified that Rice and Day were not clients of either of his firms. (5 AA 1361, 1362-1363 ["They weren't clients of Pillsbury or Nixon. That was crystal clear to me and the other folks that were working at those firms"; "there wouldn't have been letters sent to them as individuals because we weren't representing them as individuals"; "he wasn't a client"; "they weren't our clients"; "once again, he wasn't a Pillsbury client or my client"].)
- In asking the arbitrator to dismiss Rice and Day's claims with prejudice, Downs argued that he disputes "the notion" that he

or any of his firms represented Rice or Day individually "at any time" except for a specific 2010 loan transaction in which he represented Day. (5 AA 1374; see 16 AA 4423.)

- Downs continued to make these assertions in his arbitration brief and opening statements even though Rice and Day's claims had already been dismissed, arguing that Rice and Day had been "dishonest" in contending that Downs' firms had represented them and that this "impacts on [Rice and Day's] credibility." (6 AA 1438; see also e.g., 6 AA 1417 ["Rice and Day were never Downs' clients, and Rule 3-300 did not apply"], 1418 ["Rule 3-300 does not apply at all where, as here, the lawyer enters into a business transaction with someone who is not his client"].)

Rice and Day's new counsel, retained after the arbitration, ultimately discovered that Pillsbury and Nixon Peabody had each issued multiple legal opinions that unequivocally showed that the firms *did* represent Rice and Day individually. (7 AA 1874-1875.) Between October 13, 2007 and October 19, 2010, Pillsbury issued at least twelve such opinion letters to federally-insured financial institutions and government agencies regarding various affordable housing projects. (6 AA 1513, 1521-1557; 12 AA 3301-3302, 3308-3314, 3339-3346, 3360-3367.) Nixon Peabody did the same in at least eleven opinion letters between October 19, 2010 and August 2, 2012. (6 AA 1513, 1566-1577, 1619-1639.)

Each opinion letter stated that "[w]e have acted as Counsel to . . . William E. Rice, an individual ('Rice'), Gary P. Downs, an individual ('Downs'), Kristoffer J. Kaufmann, an individual ('Kaufmann'), and Douglas B. Day, an individual ('Day')" either "in connection with the acquisition, construction and rehabilitation by [HPD] of" the housing project or a loan—or similar language. (6 AA 1521, 1542-1556; 12 AA 3308, 3339, 3360; 12 AA 3308, 3339, 3360.) Many contained additional language such as: "we have been asked to render this opinion on behalf of the Co-General Partner, the Partnership, the Developer, Rice, Downs, Kaufman" and that the opinions were based on knowledge obtained "in the course of our representation of" these parties—again specifically naming Rice or referring to him by a term defined elsewhere in the letter. (E.g., 12 AA 3308, 3340, 3361.)

In response, Downs argued that despite what the opinion letters say, "neither Nixon nor Pillsbury represented Rice or Day individually in connection with the Opinion Letters or guarantees." (16 AA 4415.) He also said that neither Rice nor Day "were set up in the Nixon accounts as clients" and were never billed. (16 AA 4416.)

I. The Trial Court Partially Vacates The Award, Making Detailed Findings About Downs' Misconduct That Resulted In The Dismissal Of Rice And Day's Claims.

Downs petitioned to confirm the award. (1 AA 18-24.) Rice and Day filed a timely petition seeking vacatur only to the extent that the

arbitrator had converted their dismissal without prejudice into a dismissal with prejudice. (2 AA 370-395.) They argued that the parties' agreement effectively prohibited that remedy. (*Ibid.*) After filing the petition to partially vacate the award, Rice and Day's new trial counsel discovered the opinion letters that contradict Downs' repeated statements that he never represented Rice and Day. (8 AA 1874; pp. 29-30, *ante*.) Rice and Day then filed a reply brief and supplemental papers arguing that the award should also be vacated because it was procured by "fraudulent and undue means"—through a combination of perjury and discovery delays. (5 AA 1285-1294; 7 AA 1855-1866; see 3 RA 750-768 [slide presentation showing contradictions].) On October 22, 2014, after a lengthy hearing (7 AA 1739-1827), the trial court ordered supplemental briefing regarding the opinion letters and the conversion of the dismissals into dismissals with prejudice (7 AA 1828-1847). Both sides provided voluminous evidence and argument on their competing versions of the events that transpired in discovery.[2]

On February 2, 2015, the trial court issued a lengthy order vacating the award to the extent that Rice and Day had requested. (16 AA 4406-4431.) Following detailed factual findings that Downs and Nixon Peabody engaged in a "coordinated campaign" to delay and deny discovery and that

[2] Downs supplied evidence and argument contending that he and Nixon Peabody did nothing wrong—that any delay or lack of discovery was the fault of Rice and Day's arbitration counsel. (E.g., 4 AA 917-920, 941-942; 14 AA 3815-3816, 3947-3951; 15 AA 3974-3978, 4212.) Rice presented evidence to the contrary. (E.g., 12 AA 3166-3299.)

this resulted in the dismissal with prejudice (16 AA 4419-4421), the court concluded that "justice requires" vacatur because "it is unjust to punish Rice and Day for their attorney's choice to dismiss, without prejudice, when he would not have done so had he any idea that the dismissal, without prejudice, would be converted to a dismissal, with prejudice" (16 AA 4428-4429). The court determined that the dismissal must be converted back into a dismissal without prejudice so that Rice and Day could have the opportunity to commence an arbitration to decide the merits of their malpractice and fiduciary claims. (16 AA 4429-4430.)

Accordingly, the court (1) vacated the award to the extent that it dismissed Rice and Day's claims with prejudice and (2) confirmed the remainder of the award. (16 AA 4430.)

The court, however, rejected some of Rice and Day's other bases for vacatur.

First, the court rejected vacatur based on perjury—Down's false testimony that he never represented Rice and Day individually—because:

- Rice and Day could not establish the willfulness element of perjury by clear and convincing evidence; the court thought that Downs might have "reasonably understood" that his firms did not represent the individuals given the lack of a retainer agreement and bills to the individuals. (16 AA 4417, 4423.)
- The award could not be vacated for perjury because the opinion letters—the linchpin of the perjury charge—were available to

Rice and Day's former counsel before he moved to dismiss the arbitration claims. (16 AA 4417-4419, 4421, 4423-4424.)

Second, the court rejected Rice and Day's argument that the arbitrator had no power to convert the dismissal without prejudice into a dismissal with prejudice. (16 AA 4424-4428.)

J. The Pending Arbitration Against Downs And Litigation Against Nixon Peabody.

As a result of the events described above, Rice and Day have still never presented their fiduciary duty claims or even had a meaningful opportunity to conduct discovery. Per the trial court's suggestion, Rice and Day re-filed their claims against Downs in a new arbitration; the arbitration of those claims has since been stayed pending this appeal. (16 AA 4429; 4/29/15 Letter to Court; Preliminary Response to Writ Petition, p. 6 (B263126).)

Rice and Day's overlapping suit against Nixon Peabody remains stayed.

K. Judgment; Statement of Appealability.

Because of some questions about appealability, both sides filed two notices of appeal.

First notices. On February 3, 2015, the trial court entered its order partially vacating the award. (16 AA 4406-4431.) Three days later, Downs filed his notice of appeal from that order. (16 AA 4432-4464.) Rice did the same on March 30, 2015, appealing to the extent that the order rendered

final and appealable the earlier order compelling arbitration. (3 RA 772-773.)

Second notices. On June 1, 2015, the trial court entered judgment. (18 AA 4722-4725.) Downs served notice of entry of judgment on June 5, 2015 (18 AA 4719, 4804-4805) and Downs filed a notice of appeal on June 12, 2015 (18 AA 4806-4808). Rice filed a timely notice of appeal on June 19, 2015. (3 RA 776-777.)[3]

The order compelling arbitration became appealable upon entry of judgment. (*State Farm Fire & Casualty, supra,* 211 Cal.App.3d at p. 506 [orders compelling arbitration are not immediately appealable, but are appealable following judgment confirming the award].)

[3] Although Day also appealed, he dismissed that appeal on August 3, 2015.

CROSS-APPELLANT'S OPENING BRIEF

The cross-appeal issues both logically precede and moot the issues raised in Downs' appeal. We will demonstrate that Rice and Day's claims should never have been ordered to arbitration in the first place and that Rice and Day therefore should never have been confronted with any of the dismissal issues now before this Court.

Those claims have yet to be litigated in any forum. Reversal of the order compelling arbitration will put them back where they belong—in the trial court, where at long last Rice will have a hearing on the merits of his claims against Downs and Nixon Peabody.

STANDARDS OF REVIEW

Scope of arbitration agreement. Where, as here, there is no conflicting extrinsic evidence, the court reviews de novo the proper interpretation of an arbitration agreement and whether particular claims are arbitrable. (*Bono v. David* (2007) 147 Cal.App.4th 1055, 1061-1062 (*Bono*).)

Statutory exception to arbitration. The ultimate decision whether to stay or deny arbitration under section 1281.2(c) is reviewed for abuse of discretion. (*Daniels v. Sunrise Senior Living, Inc.* (2013) 212 Cal.App.4th 674, 680.)

It is less clear what standard applies to the issue presented here—the threshold determinations regarding whether the statute applies. But at least under our facts, review should be de novo.

Some courts have explained that the trial court's discretion "does not come into play until it is ascertained that the subdivision applies . . . ." (E.g., *ibid.*) Those courts hold that analysis of the threshold requirements involve questions about "the proper interpretation and application of section 1281.2, subdivision (c)" that are reviewed de novo. (*Birl v. Heritage Care LLC* (2009) 172 Cal.App.4th 1313, 1318.) Other courts have stated that they review the "trial court's determination whether there is a possibility of conflicting rulings on a common issue of law or fact for abuse of discretion." (*Lindemann v. Hume* (2012) 204 Cal.App.4th 556, 565; see also *Metis Development LLC v. Bohacek* (2011) 200 Cal.App.4th 679, 691.) Still others state that "[w]hether there are conflicting issues arising out of related transactions is a factual determination subject to review under the substantial evidence standard." (*Acquire II, Ltd. v. Colton Real Estate Group* (2013) 213 Cal.App.4th 959, 972.)

We see no reason why the existence of a "possibility" of conflicting rulings involve any exercise of discretion, and it would be a rare case that required factual findings. No evidentiary showing is required to establish a "possibility" of conflicting rulings, which is necessarily a function of what the pleadings allege. (*Abaya v. Spanish Ranch I, L.P.*, (2010) 189 Cal.App.4th 1490, 1498-1499 (*Abaya*).) An overlap either does or doesn't exist based on the nature of the allegations. And, like review of a demurrer, this Court can review the allegations of a complaint as a matter of law.

Here, no one suggested that the trial court needed to go beyond the pleadings to determine the possibility of conflicting rulings. In fact, the

parties agreed that the possibility existed. That should mean de novo review.

ARGUMENT

The Court should reverse the order compelling arbitration for two independent reasons: (1) Most of the claims against Downs are not within the scope of the narrow arbitration clause; (2) even if the claims were arbitrable, the trial court erred in failing to consider its power to deny arbitration pursuant to statute.

I. RICE'S TORT CLAIMS AGAINST DOWNS ARE NOT ARBITRABLE.

A. Determining The Scope Of An Arbitration Clause.

1. General principles.

Two critical principles guide the determination of whether a particular claim is arbitrable.

Arbitration is certainly favored, so "when there is doubt as to the meaning and construction of an agreement for mediation and/or arbitration, that doubt should be resolved in favor of those processes." (*Bono*, *supra*, 147 Cal.App.4th at p. 1062.) Accordingly, the burden falls on the party opposing arbitration to demonstrate that an arbitration clause cannot cover the dispute. (*Ibid.*)

"But there is another principle that needs to be considered." (*Id.* at p. 1063.) Despite the strong public policy in favor of arbitration, "there is no public policy favoring arbitration of disputes which the parties have not

agreed to arbitrate." (*Ibid.*; see *Victoria v. Superior Court* (1985) 40 Cal.3d 734, 744 [same].) "Indeed, this principle is effectively prescribed by Civil Code section 1648, which provides: 'However broad may be the terms of a contract, it extends only to those things concerning which it appears that the parties intended to contract.'" (*Bono*, *supra*, 147 Cal.App.4th at p. 1063.) Thus, "[i]n performing its duty to determine whether a party has a contractual duty to arbitrate a particular dispute, a court is required 'to examine and, to a limited extent, construe the underlying agreement.'" (*City of Los Angeles v. Superior Court* (2013) 56 Cal.4th 1086, 1096; see *Bono, supra,* 147 Cal.App.4th at p. 1063.)

As always, the "fundamental goal" is to give effect to the intent of the parties. (*Hotels Nevada, LLC v. Bridge Banc, LLC* (2005) 130 Cal.App.4th 1431, 1435 (*Hotels Nevada, LLC*).) "[O]rdinary rules of contract interpretation apply" to determine that intent. (*Ibid.*; see *In re Tobacco Cases I* (2004) 124 Cal.App.4th 1095, 1104.)

2. Broad versus narrow arbitration clauses.

"As secondary authorities which analyze many [of the key cases] strongly suggest, the decision as to whether a contractual arbitration clause covers a particular dispute rests substantially on whether the clause in question is 'broad' or 'narrow.'" (*Bono, supra,* 147 Cal.App.4th at p. 1067, citing Knight et. al., Cal. Practice Guide, Alternative Dispute Resolution (The Rutter Group 2005) ¶ 5:215.3.)

The "usual," "most common 'broad form' arbitration agreement covers '. . . all claims or disputes *arising out of or relating to* this agreement or breach thereof.'" (Knight et. al., Cal. Practice Guide, Alternative Dispute Resolution (The Rutter Group 2014) ¶ 5:215.4, original italics.) Such broad clauses strengthen the presumption of arbitrability. (*Id.* at ¶ 5:222.) Parties electing to use the classic broad formulation—"arising out of or related to"—presumably intend a broader scope than those that merely cover claims "arising out of" the agreement. After all, the former includes two classes of claims: (1) claims that arise out of the agreement, and (2) claims that *do not* arise out of, but *are* related to, the agreement.

Other common broad formulations use a single clause that is inherently broader than contract claims, such as agreements to arbitrate any claims "*in connection* with this Agreement." (E.g., *Izzi v. Mesquite Country Club* (1986) 186 Cal.App.3d 1309, 1315-1317 (*Izzi*), italics added; *Simula, Inc. v. Autoliv, Inc.* (9th Cir. 1999) 175 F.3d 716, 720 & fn. 3 (*Simula, Inc.*) [distinguishing agreement covering claims "arising in connection" with the agreement from the more narrow "arising under" or "arising out of"].)

Courts have consistently held that the broader formulations express an intent to arbitrate not just contract claims, but also tort claims that have their roots in the relationship that was created by the contract or in the formation of the contract. (E.g., *Bos Material Handling, Inc. v. Crown Controls Corp.* (1982) 137 Cal.App.3d 99, 104 (*Bos Material Handling*,

Inc.) ["arising out of or relating to" the agreement]; *Berman v. Dean Witter & Co., Inc.* (1975) 44 Cal.App.3d 999, 1003 (*Berman*) [same]; *Izzi, supra,* 186 Cal.App.3d at pp. 1315-1317 [claims "in connection with this Agreement"]; *Simula, Inc., supra,* 175 F.3d at p. 720 & fn. 3 [same].)

"More narrowly worded clauses" are "dangerous" to the party seeking to arbitrate a particular claim. (Knight et. al., Cal. Practice Guide, Alternative Dispute Resolution, *supra,* ¶ 5:223; *Bono, supra,* 147 Cal.App.4th at p. 1067.) "For example, a clause covering 'any dispute *arising from* this agreement' may cover only *contractual* disputes, whereas a clause covering disputes 'arising from or *related to*' the agreement would also cover misconduct in performance of the contract (tort claims)." (Cal. Practice Guide, *supra,* ¶ 5:223, original italics.)

Thus, California courts and the Ninth Circuit have repeatedly found "arising out of" and similar formulations to be narrower than "arising out of or related to"—and therefore not intended to cover tort claims. (E.g., *Cobler v. Stanley, Barber, Southard, Brown & Assoc*. (1990) 217 Cal.App.3d 518, 530 [arbitration agreements covering disputes "arising from this Agreement" are "generally considered to be more limited in scope than would be, for example, a clause agreeing to arbitrate 'any controversy . . . arising out of *or relating to* this agreement,' which might thus cover misconduct arising out of the agreement as well as contractual issues," italics and ellipses in original]; *Hall v. Superior Court* (1993) 18 Cal.App.4th 427, 435 [distinguishing *Cobler* because arbitration clause in *Hall* governed "'any dispute or claim in law or equity arising out of this

contract or any resulting transaction'"]; *Dream Theater, Inc. v. Dream Theater* (2004) 124 Cal.App.4th 547, 553, fn. 1 (*Dream Theater*) ["omission of the phrase *or relating to* has been found to exclude arbitration of some claims," italics in original]; *Mediterranean Enterprises, Inc. v. Ssangyong Corp.* (9th Cir. 1983) 708 F.2d 1458, 1464 ["We have no difficulty finding that 'arising hereunder' is intended to cover a much narrower scope of disputes, *i.e.*, only those relating to the interpretation and performance of the contract"]; *Tracer Research Corp. v. National Environmental Serv. Co.* (9th Cir. 1994) 42 F.3d 1292, 1294-1295 ["Notwithstanding the federal policy favoring" arbitration, parties "narrowly circumscribe[]" the scope of arbitration by covering only claims "arising out of" the agreement]; *Cape Flattery Ltd v. Titan Maritime, LLC* (9th Cir. 2011) 647 F.3d 914, 922-923 (*Cape Flattery Ltd.*) [although doubts concerning the scope of an agreement must be resolved in favor of arbitration, "arising hereunder," "arising under," and "arising out of" are relatively narrow clauses].) As the Ninth Circuit has repeatedly explained, it is "significant" when parties omit reference to the additional class of claims that "relate to" the agreement and instead only cover claims "arising out of" or "arising from" the agreement. (*Mediterranean Enterprises, Inc., supra*, 708 F.2d at pp. 1463-1464; *Tracer Research Corp., supra*, 42 F.3d at pp. 1294-1295; *Cape Flattery Ltd., supra*, 647 F.3d at pp. 922-923.)

Our research has not disclosed a single California or Ninth Circuit case holding that agreements requiring arbitration of "claims arising out of the agreement"—without additional contractual language—include tort

claims. (Some federal courts, however, differ in their interpretation under federal law. See p. 48, *post*; *EFund Capital Partners v. Pless* (2007) 150 Cal.App.4th 1311, 1328-1330 (*EFund*) discussed at pp. 52-54, *post*.)

In any event, as we next demonstrate, the academic debate about the *general* meaning of the term "arising out of" is irrelevant here. The Court need not consider whether, as a *general* matter, "arising out of" should have the same broad meaning as "arising out of or related to" and other broad formulations. Instead, this case is controlled by other contract language and basic principles of contract interpretation that make clear that the parties to the operating agreements intended "arising out of" to have a narrow meaning.

B. The Parties Agreed On A Narrow Arbitration Clause That Requires Arbitration Only Of Contract Disputes—Not Tort Claims.

1. The contract's express language shows that the parties intended to narrowly circumscribe the scope of arbitrable issues.

This is not an arbitration agreement that simply uses the phrase "arising out of" without any further context. Another provision of the agreement demonstrates that *these* parties intended "arising out of" to have a narrow meaning.[4]

[4] Rice did not raise this additional contractual provision below, although he urged other reasons to narrowly interpret the scope of the arbitration clause. (continued. . .)

Courts interpret arbitration agreements by applying the "ordinary rules of contract interpretation." (*Hotels Nevada, LLC, supra,* 130 Cal.App.4th at p. 1435; *In re Tobacco Cases I, supra,* 124 Cal.App.4th at p. 1104.) That means that courts do not determine the parties' intent from an isolated clause. (*Transportation Guarantee Co. v. Jellins* (1946) 29 Cal.2d 242, 247; *Epic Communications, Inc. v. Richwave Technology, Inc.* (2015) 237 Cal.App.4th 1342, 1349.) Rather, contracts must be construed as a whole, with "each clause helping to interpret the other." (*Epic Communications, Inc., supra,* 237 Cal.App.4th at p. 1349; Civ. Code, § 1641; see *Lemm v. Stillwater Land & Cattle Co.* (1933) 217 Cal. 474, 480 [same].)

Here, paragraph 13.4—the paragraph that immediately precedes the arbitration clause—dispositively clarifies the parties' intent:

Paragraph 13.4. This paragraph broadly requires the parties to consent to the jurisdiction of California state and federal courts regarding the full range of claims that are connected with the operating agreements and the parties' relationship. It does this by using multiple phrases to convey that broad range of claims:

(. . . continued)

However, neither side has ever suggested that any extrinsic evidence illuminates the breadth of the arbitration clause. So, this argument poses a pure question of law based on the undisputed language of the operating agreements. (*In re Marriage of Rosenfeld and Gross* (2014) 225 Cal.App.4th 478, 485 [absent extrinsic evidence, contract interpretation is a question of law].) A party may raise a new theory on appeal where it involves a purely legal question. (*Dieckmeyer v. Redevelopment Agency of City of Huntington Beach* (2005) 127 Cal.App.4th 248, 259.) Moreover, there can be no prejudice from considering the argument: the parties have not arbitrated or litigated Rice's claims.

> Each member hereby consents to the exclusive jurisdiction of the state and federal courts sitting in California in any action on a claim *arising out of, under or in connection with this Agreement or the transactions contemplated by this Agreement*.

(1 RA 110 at ¶ 13.4, italics added.)[5] Together, these multiple phrases cover claims having anything whatsoever to do with the parties' contractual relationship. The parties must have thought that "arising out of" was not enough to cover that full range. In fact, any other interpretation would inappropriately render much of the language mere surplusage. (*Jones v. Jacobson* (2011) 195 Cal.App.4th 1, 18 (*Jones*) [courts "should give effect to every provision and avoid rendering any part of an agreement surplusage"]; *Segal v. Silberstein* (2007) 156 Cal.App.4th 627, 633 [same].)

Paragraph 13.5. The parties approached arbitration differently. They only agreed to arbitrate a subset of the claims described in paragraph 13.4:

> Except as otherwise provided in this Agreement, any controversy between the parties *arising out of this Agreement* shall be submitted to the American Arbitration Association for arbitration in Los Angeles, California or San Francisco, California.

[5] The original operating agreement contains the identical language. (1 RA 74 at ¶ 12.4.)

(1 RA 110 at ¶ 13.5, italics added.)[6]

Interpreting the contract as a whole, the neighboring provision forecloses whatever abstract debate exists about what other parties might mean by the phrase "arising out of." *These* parties did not intend *their* arbitration agreement to cover the entire broad range of claims—the range as described in the preceding paragraph. *These* parties intended to arbitrate only a narrow subset of claims: only claims "arising out of this Agreement," but not claims "under or in connection with this Agreement or the transactions contemplated by this Agreement." A sophisticated firm like Pillsbury presumably knew better than to try to use a single phrase—"claims arising out of"—to express different things in neighboring contract paragraphs. And the parties presumably appreciated the difference in the two neighboring clauses as well. The choice was intentional.

The particular omission further establishes that the parties intended the choice that they made. At the time of their agreement, the language they omitted from their arbitration clause was language that courts had repeatedly held sufficiently broad to encompass tort claims. Courts had already held that a contract requiring arbitration of claims "in connection with this Agreement" encompassed tort claims. (*Izzi*, *supra*, 186 Cal.App.3d at pp. 1315-1317; *Dream Theater*, *supra*, 124 Cal.App.4th at p. 553, fn. 1; *Simula, Inc.*, *supra,* 175 F.3d at p. 720 & fn. 3.) Here, the parties used that exact language to describe claims that were to be subject to

[6] The original operating agreement contains this same arbitration language. (1 RA 74 at ¶ 12.4.)

jurisdiction in state or federal *court* in California—they wanted tort claims to be litigated in California. (1 RA 110 at ¶ 13.4.) But they conspicuously omitted that same language in their arbitration clause. (1 RA 110 at ¶ 13.5.)

* * * * *

Words have meaning. The omission of words likewise has meaning. The policy favoring arbitration cannot trump contractual language expressing the parties' intent to arbitrate only a narrow class of claims. (*Bono, supra,* 147 Cal.App.4th at p. 1063.)

2. Even without paragraph 13.4, the arbitration clause calls for a narrow interpretation.

As shown above (pp. 39-41, *ante*), California courts, the Ninth Circuit and practice guides have repeatedly recognized a distinction between arbitration clauses that cover claims "arising out of" an agreement and those that cover claims "arising out of or related to" an agreement. One must assume that knowledgeable California transactional lawyers look to these authorities for guidance in crafting arbitration clauses. This too presents an independent basis to reverse the order compelling arbitration.

a. Upholding the distinction is consistent with the rules of contract interpretation.

The fundamental rules of contract interpretation mandate upholding the often-repeated distinction between "arising out of" and "arising out of

or relating to." (See p. 38, *ante* [courts apply ordinary rules of contract interpretation].)

Courts "should give effect to every provision and avoid rendering any part of an agreement surplusage." (*Jones*, *supra*, 195 Cal.App.4th at p. 18.) This rule requires attributing different meanings to the two clauses in "arising out of *or* relating to this agreement," with the use of "or" indicating that the parties intended a broader meaning than either clause alone conveys. Moreover, these are well-known formulations of arbitration clauses. When parties select the more limited phrase, "arising out of," they cannot have intended it to embrace everything included by the two separate phrases in the common, broad-form arbitration clause.

b. Upholding the distinction is necessary to carry out the intent of California parties and their attorneys, who rely on a distinction that courts have reiterated for decades.

It is also reasonable, if not imperative, to consider that California parties and their attorneys have come to rely on the long-repeated distinction. Their intent would be thwarted if a different interpretation were announced now.

For decades, California courts and the leading practice guide have repeatedly instructed that the two formulations are significantly different. (See pp. 39-41, *ante*.) For decades, the Ninth Circuit—the federal jurisdiction that most frequently reviews and construes the scope of

California arbitration clauses—has said the same. (See pp. 40-41, *ante*.) Indeed, this distinction in the arbitration cases is so pervasive in California that at least one California court relied on them when interpreting similar language in an unrelated statute. (*MHC Financing Ltd. Partnership Two v. City of Santee* (2005) 125 Cal.App.4th 1372, 1398 [interpreting Mobilehome Residency Law].)

"Once they know the specific language that is required, [contracting parties] can rely on that language to produce a result they jointly desire." (*Cape Flattery Ltd., supra,* 647 F.3d at p. 923.) To paraphrase *Cape Flattery Ltd.*, "[t]here is no reason to believe that the experienced lawyers" who advised the parties here and who drafted the HPD operating agreements "intended that the language they chose would be interpreted differently than it had been" in California. (*Ibid*.)

The Second Circuit's application of this parties-expectations approach is instructive. Like the Ninth Circuit, the Second Circuit recognizes a "need to protect the intent of the parties" who presumably relied on past articulations of the difference between the language of various arbitration clauses. (*S.A. Mineracao Da Trindade-Samitri v. Utah International, Inc.* (2d Cir. 1984) 745 F.2d 190, 194 (*S.A. Mineracao*).) While the Ninth Circuit's narrow interpretation of "arising out of" is currently the minority view among federal circuits applying federal law (*Dialysis Access Center, LLC v. RMS Lifeline, Inc.* (1st Cir. 2011) 638 F.3d 367, 381), and while the Second Circuit, which previously agreed with the Ninth Circuit (*In re Kinoshita* (2d Cir. 1961) 287 F.2d 951, 952-953) has

since questioned it, the Second Circuit has recognized that regardless of what interpretation it might reach if it were writing on a clean slate, it would defeat parties' intent to shift interpretations that it had already articulated (*S.A. Mineracao, supra*, 745 F.2d at p. 194). Courts need to be "concerned that contracting parties may have (in theory at least) relied on [prior judicial interpretations] in their formulation of an arbitration provision." (*Ibid.*) Accordingly, the Second Circuit has held that an arbitration clause must be narrowly interpreted when parties evidence that they intended a narrow scope by using contractual language that courts had previously recognized as narrow. (*Ibid.*) The Fifth Circuit has implied the same thing. (*Mar-Len of Louisiana, Inc. v. Parsons-Gilbane* (5th Cir. 1985) 773 F.2d 633, 637 [citing *S.A. Mineracao, supra,* and broadly interpreting arbitration clause because it differed from the form that the Second Circuit had previously interpreted narrowly].)

Had the parties wanted a broad clause, they easily could have chosen the common broad form. Instead, in 2003, they agreed on the narrower formulation for their arbitration clause—"arising out of." (1 RA 74 at ¶ 12.5.) In 2007, they adhered to that language in the amended operating agreement. (1 RA 110 at ¶ 13.5.) Their intent should not be frustrated.

c. Downs' contrary arguments are meritless.

We expect Downs to urge what he urged below: that California and federal cases applying California law are "directly on point" in holding

"that the 'arising out of' language was broad enough to encompass related tort claims." (2 RA 532.)

It's just not true.

First, Downs argued that a federal district court decision, *Bosinger v. Phillips Plastics Corp.* (S.D.Cal. 1999) 57 F.Supp.2d 986, 993-994, applied California law and held that it was "enough" that the arbitration clause required arbitration of claims "'arising out of'" the agreement—that this language alone covered tort claims. (2 RA 532.) The trial court agreed with Downs, saying that "the Court will follow the *Bosinger* case's ruling that 'arising out of' is broad enough to encompass tort causes of action." (3 RA 745.)

But those were not *Bosinger*'s facts or ruling—not even close. The *Bosinger* court emphasized that the arbitration clause before it was broader than "arising out of": It required arbitration of "'any dispute, controversy, or claim arising out of *or relating to this Agreement or the relationship between the parties*." (*Bosinger, supra*, 57 F.Supp.2d at p. 988, italics added.) The court compelled arbitration of tort claims precisely because the agreement used the broader, "related to" form. (*Id.* at p. 993.) It could not have been more explicit: "In comparison to an arbitration clause utilizing the language 'arising out of,' which is construed to apply only to a narrow range of disputes specifically relating to the interpretation and performance of the contract at issue, courts interpret an arbitration

provision containing the language 'arising out of and or relating to' as a 'broad arbitration clause.'" (*Ibid.*)[7]

Second, Downs claimed that "several California cases [are] directly on point" in holding that an arbitration agreement need only include the "arising out of" language to encompass tort claims. (2 RA 532, italics omitted.) He offered three such supposed cases. But, as with *Bosinger*, it just isn't true:

- The arbitration agreement in *Berman, supra*, 44 Cal.App.3d at p. 1003 (cited at 2 RA 532) included the broad "related to" language. It held that the "phrase 'any controversy . . . arising out of *or relating to* this contract . . .' is certainly broad enough to embrace tort as well as contract liabilities . . . ." (44 Cal.App.3d at p. 1003, italics added, ellipses in original.)

- The same is true of *Bos Material Handling, Inc., supra*, 137 Cal.App.3d 99 (cited at 2 RA 532): the clause required arbitration of "[a]ny controversy or claim arising out of *or relating to* this agreement." (137 Cal.App.3d at p. 104, italics added.) The court held that "[i]n the particular situation where contracts provide arbitration for 'any controversy . . . arising out of or relating to the contract . . .' the courts have held such

[7] In dictum, *Bosinger* cited a Seventh Circuit decision holding that the language "arising out of" is sufficient. (*Ibid.*) But the court gave no indication that it was following that precedent or why it would be necessary to do so given that the arbitration agreement before it employed the classic broad formulation.

arbitration agreements sufficiently broad to include" certain tort claims. (*Id.* at p. 105, ellipses in original.)

- *Coast Plaza Doctors Hospital v. Blue Cross of California* (2000) 83 Cal.App.4th 677 (*Coast Plaza*) (cited at 2 RA 532) likewise does not hold that it is enough that the agreement covers claims "arising out of" the agreement. There, the arbitration agreement covered "[a]ny problem or dispute arising under this Agreement *and/or concerning the terms of this Agreement* . . . ." (83 Cal.App.4th at pp. 681, fn. 2, 684, italics added.) While slightly different from the more common "related to" formulation, this clause unquestionably broadened the arbitrable disputes beyond those that "[arose] under" the agreement. (Cf. *Simula, Inc., supra,* 175 F.3d at p. 720 & fn. 3 [distinguishing agreement covering claims "arising in connection" with the agreement from the narrower "arising under" or "arising out of"].) Thus, *Coast Plaza* held that the agreement was sufficient to cover the particular tort claims, which were "inextricably related to [the contract's] terms and provisions." (83 Cal.App.4th at pp. 684-686 [the plaintiff claimed that the other contracting party tortiously refused to renegotiate the contract's reimbursement rates].)

Third, Downs repeatedly relied on *EFund*, *supra*. (1 RA 27, 36; 2 RA 531-533.) But *EFund* does not hold that the language "arising out of"

is alone sufficient to require arbitration of tort claims or claims involving the formation of an agreement.

In *EFund*, the arbitration clause covered all disputes "arising *from or out of*" agreement. (150 Cal.App.4th at p. 1322, italics added.) While the substantive difference between these two phrases is not entirely clear, the *EFund* parties must have intended something broader than what either clause would separately cover. The Court of Appeal emphasized that the "crucial language" in the arbitration clause "differs from that discussed" in two Ninth Circuit cases that interpreted "arising out of" narrowly: "The critical language in the two Ninth Circuit opinions were 'arising hereunder' in *Mediterranean Enterprises, Inc.* [*supra*, 708 F.3d 1458] and 'arising out of this Agreement' in *Tracer Research* [*supra*, 42 F.3d 1292]. By contrast, the language in the arbitration clause in [*EFund*] is materially broader—'arising from or out of'—than that in *Mediterranean Enterprises, Inc.* or *Tracer Research*." (*Id.* at p. 1328, citations omitted.) Not surprisingly, the trial court did not rely on, or even cite, *EFund*. (3 RA 736-749.)

In dictum, *EFund* also opined that those Ninth Circuit cases were out of step with the modern federal and state rule requiring liberal construction of arbitration awards. (*Id.* at pp. 1328-1330.) But, as the Ninth Circuit has since made clear, drawing a distinction between arbitration clauses covering claims "arising out of" and those covering "arising out of or relating to" is perfectly consistent with the required preference for arbitration. (*Cape Flattery Ltd.*, *supra*, 647 F.3d at pp. 922-923.) It merely recognizes that there is no policy in favor of compelling arbitration of

claims that the parties did not agree to arbitrate and that courts must respect the parties' choice to use more limited language. (See pp. 37-38, *ante*.)

In any event, *EFund*'s dictum is not entitled to substantial weight. The *EFund* parties did not brief, and the Court of Appeal did not address, any of the key issues argued here, including the significance of presumed reliance on previous interpretations by California courts and federal courts sitting in California. (Pp. 47-49, *ante*.) Nor did the Court of Appeal (or any of the federal cases on which it relied) explain how ordinary rules of contract interpretation permitted interpreting the two clauses "arising out of" and "related to" as duplicative surplusage. (Pp. 46-47, *ante*.) In fact, the parties' briefs in *EFund* barely scratched the surface in discussing the Ninth Circuit and other federal cases.[8]

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[8] "'Reference to briefs is a permissible method of ascertaining what issues were before a court.'" (*McAdory v. Rogers* (1989) 215 Cal.App.3d 1273, 1277, citations omitted; see also *Moore v. Superior Court* (1970) 13 Cal.App.3d 869, 873-874 [interpreting decision in light of issues raised in appellate briefs].)

In *Efund*, the entire thrust of the opening and reply briefs was that the agreement included tort claims because the arbitration provision was crucially broader than those that simply included claims "arising out of" the agreement. (Appellants' Opening Brief, 2007 WL 540269 at *7-10; Reply Brief, 2007 WL 953268 at *4-7.) Other than distinguishing the contractual language, the opening brief devoted just two sentences to the analysis of the Ninth Circuit cases, observing only that other circuits disagreed with the Ninth Circuit. (Appellants' Opening Brief, 2007 WL 540269 at *8-9.) The reply brief did not mention the federal cases, except in footnotes that merely stated that the Ninth Circuit cases were not binding. (Reply Brief, 2007 WL 953268 at *4-6, fns. 2-3.) The respondent's brief, for its part, only cited California and Ninth Circuit authority and claimed that there was no circuit split at all. (Respondent's Brief, 2007 WL 2972178 at *7-12.) Neither party raised the arguments presented here—about ordinary rules of contract interpretation or the impact of party expectations based on prior court pronouncements.

* * * * *

The parties agreed on a classically narrow arbitration clause. The Court should interpret it as courts have consistently instructed California parties and attorneys to interpret it: narrowly. (§ I.B.2., *ante*.)

But the Court can easily decide this case even without reaffirming the general rule that "arising out of" should be interpreted narrowly. Here, the agreement as a whole makes clear that *these parties* intended a narrow arbitration clause that does not include tort claims. (§ I.B.1., *ante*.) Either way, the order compelling arbitration must be reversed.

II. EVEN IF RICE'S CLAIMS WERE ARBITRABLE, THE TRIAL COURT NEVERTHELESS COMMITTED REVERSIBLE ERROR IN ORDERING THE CLAIMS TO ARBITRATION.

Reversal is required even if all of Rice and Day's claims against Downs were arbitrable. The arbitration against Downs and the litigation against Nixon Peabody undeniably involved common factual or legal issues concerning the fiduciary duty claims, creating a possibility of inconsistent results. Indeed, both Downs and Nixon Peabody conceded as much. By statute, that commonality triggered the trial court's discretion to deny enforcement of the arbitration agreement. Nixon Peabody even urged the trial court to deny arbitration as to the malpractice and fiduciary duty claims.

But the trial court never exercised that discretion because it erroneously believed that there was no statutory basis for doing so. This failure to exercise discretion is itself a reversible abuse of discretion. (E.g., *People v. Orabuena* (2004) 116 Cal.App.4th 84, 99 (*Orabuena*).)

A. A Court May Deny A Petition To Compel Arbitration When There Is A "Possibility" Of Conflicting Rulings On Factual Issues Common To Both The Arbitration And A Lawsuit With A Third Party.

Ordinarily, Code of Civil Procedure section 1281.2 requires courts to compel arbitration if the parties agreed to arbitrate the controversy. But there are exceptions, and one of them—section 1281.2(c)—applies here.

"Section 1281.2(c) addresses the peculiar situation that arises when a controversy also affects claims by or against other parties not bound by the arbitration agreement." (*Cronus Investments, Inc. v. Concierge Services* (2005) 35 Cal.4th 376, 393 (*Cronus*).) It provides that courts can deny arbitration when [1] a "party to the arbitration agreement is also a party to a pending court action or special proceeding with a third party, arising out of the same transaction or series of related transactions and [2] there is a possibility of conflicting rulings on a common issue of law or fact."

The Legislature crafted the exception "in order to avoid potential inconsistency in outcome as well as duplication of effort." (*Cronus*, *supra*, 35 Cal.4th at p. 393.) Our courts have described this policy as "equally compelling" as the strong public policy favoring arbitration and as

"consistent with the policy of encouraging arbitration." (*Abaya, supra*, 189 Cal.App.4th at p. 1497; *Fitzhugh v. Granada Healthcare & Rehabilitation Center, LLC* (2007) 150 Cal.App.4th 469, 475.) That is hardly surprising: Parties would be discouraged from signing arbitration agreements if it meant there would be wasteful, duplicative proceedings every time someone needed to arbitrate a claim against one party and litigate the same issues against another.

Because the statute is triggered by a "'*possibility*' of conflicting rulings on legal or factual issues," no evidentiary showing is required. (*Abaya, supra*, 189 Cal.App.4th at pp. 1498-1499, italics added.) Instead, the trial court examines the allegations of the complaint to determine whether there is such a possibility. (*Id.* at p. 1499.)

When section 1281.2(c) applies, courts have discretion to (a) deny arbitration on some or all issues and order that they be resolved along with the litigation involving the third party; (b) stay the arbitration pending resolution of the litigation; or (c) stay the litigation pending resolution of the arbitration. (Civ. Proc. Code, § 1281.2.) The court's discretion, however, "does not come into play until it is ascertained that the subdivision applies . . . ." (*Daniels, supra*, 212 Cal.App.4th at p. 680.)

B. It Is Beyond Dispute That Section 1281.2(c) Applies Here—Indeed, Both Downs And Nixon Peabody Conceded That The Threshold Requirements Were Met.

The complaint's allegations unquestionably demonstrate that section 1281.2(c) applies: The breach of fiduciary duty claims against Downs (a party to the arbitration agreement) and Nixon Peabody (a third party) overlap almost completely. Indeed, Nixon Peabody's liability is premised in large part on Downs' liability and involves the same factual issues. This circumstance yields numerous common issues of fact and law and unquestionably gives rise to the "possibility" that an arbitrator and jury might reach different conclusions.

Both defendants—Downs and Nixon Peabody—conceded this.

1. As the trial court found, Nixon Peabody is a "third party" within the meaning of section 1281.2(c).

It is undisputed, and the trial court found, that Rice and Day's suit against Nixon Peabody is a "pending court action or special proceeding with a third party." (§ 1281.2(c).)

"For purposes of the statute, a third party is one who is neither bound by nor entitled to enforce the arbitration agreement." (*Daniels*, *supra*, 212 Cal.App.4th at p. 679.) In the trial court's words, "Nixon Peabody [is a] third part[y] not a part of" the original or amended operating agreements, which contain the arbitration agreement. (3 RA 746.) The operating agreement defines the relationship among the members of HPD,

whereas "Nixon Peabody, LLC is an outside party." (3 RA 747; see also 1 RA 39 [Downs' petition explaining that Nixon Peabody is not subject to an arbitration agreement]; 2 RA 371, 377 [Rice and Day's brief; same], 511 [Nixon Peabody's brief; same]; 3 RA 718 [Downs' reply brief; same].)

2. The Nixon Peabody litigation and Downs arbitration concern the same series of transactions and there is a "possibility" of conflicting rulings on common issues of law and fact.

It is also undeniable that the fiduciary duty claims against Downs and Nixon Peabody arise from the same transactions and pose a "possibility" of conflicting rulings on any of the numerous common issues of fact or law. Both defendants' liability is premised on Downs' alleged misconduct—undertaken both "individually and acting as a partner of the law firm Nixon Peabody." (1 RA 12-14; see p. 18, *ante*.) For instance:

- Downs caused HPD to engage in detrimental financial transactions "[f]or his own personal benefit, and the benefit of other clients of his and of Nixon Peabody." (1 RA 13-14 at ¶ 25.e.)
- Downs and Nixon Peabody failed to comply with Rule 3-300 on multiple occasions over several years. (1 RA 13 at ¶ 25.a-25.b.)
- Downs caused other Nixon Peabody attorneys to interfere with transactions that Nixon Peabody was handling, causing

hundreds of thousands of dollars of damages and added expenses. (1 RA 13 at ¶ 25.c.)

Indeed, the only circumstance where there is no overlap is the drafting of the operating agreements, because Downs was then still a partner at Pillsbury. (1 RA 9-12 at ¶¶ 21.a.-c., 22.)

These common allegations are more than enough to trigger section 1281.2(c). In fact, they trigger the statute over and over again.

First, the claims against Downs and Nixon Peabody "aris[e] out of the same transaction or series of related transactions"—Downs' actions, if proven, create liability for both. (Code Civ. Proc., § 1281.2(c).)

Second, the overlap creates a possibility of conflicting rulings on numerous common issues of law or fact:

- Whether Downs engaged in any of the many alleged acts poses numerous common issues, because Nixon Peabody's liability is premised on those same allegations.
- Whether other Nixon Peabody attorneys followed Downs' directions to take harmful action (1 RA 13 at ¶ 25.c) is the flip side of whether Downs gave those instructions.
- Whether Rice and Day were clients of Downs and his firm (and thus whether they owed a fiduciary duty) is a common issue. (E.g., 1 RA 42; 2 RA 523-524; 3 RA 710-711; see pp. 22, 28, *ante*.)

- The extent to which Rice and Day were damaged by these alleged actions, as well as any apportionment between defendants, poses further common issues. (See *Birl*, *supra*, 172 Cal.App.4th at p. 1321 [impact of overlapping damages issues on section 1281.2(c) analysis].)

Under these circumstances, "[a] myriad of conflicting rulings is possible"—"[d]ifferent triers of fact in different proceedings could come to different and conflicting conclusions" on any of these factual issues. (*Ibid.*) What's more, a greater likelihood of different results exists because arbitration is an "informal process, not strictly bound by evidence, law, or judicial oversight." (See *Vandenberg v. Superior Court* (1999) 21 Cal.4th 815, 832 (*Vandenberg*).)

The events that ultimately transpired in the arbitration only underscore the problem. As the trial court found, Downs and Nixon Peabody engaged in a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their claims in arbitration. (16 AA 4420; pp. 23-26, *ante*.) Downs refused to provide relevant documents, including his own email correspondence, claiming that he had no power to provide documents held by the firm in which he was a partner. (*Ibid.*) Meanwhile, Nixon Peabody—a third party to the arbitration—went so far as to prevent service of a subpoena. (*Ibid.*) These sorts of tactics inherently impact a plaintiff's ability to prove his case and thus the factfinder's conclusions. None of this would likely have happened in a court, which has extensive powers to supervise and order compliance with discovery. That power is

more difficult to exercise—if not illusory—in an arbitration to which one of the defendants is not a party and whom the arbitrator therefore cannot effectively control or sanction. What's more, a court would likely be far less tolerant of misconduct by parties who, like Downs and Nixon Peabody, are also officers of the court. In fact, during the confirmation proceedings, the court itself interjected regarding Downs that misconduct is "particularly" inexcusable when committed by an officer of the court. (RT 27:15-16.)

The "possibility" of conflicting results exists even if the arbitration occurs first. For one thing, arbitration awards have no non-mutual collateral estoppel effect. (*Vandenberg*, *supra*, 21 Cal.4th at pp. 828-838.) Nixon Peabody—a stranger to the arbitration—could not be bound by the award. Nor could Nixon Peabody assert the award as collateral estoppel if Downs prevailed. (*Ibid.*) And even if res judicata could apply non-mutually, that too would not eliminate the "possibility" of inconsistent rulings on common factual or legal issues. If Rice and Day were to prevail against Downs in arbitration, Nixon Peabody would still not be bound by the award. So, Rice and Day would need to undertake substantial time and expense to relitigate all of the issues against Nixon Peabody, and the court or jury could reach a different conclusion than the arbitrator. In fact, Downs conceded as much: "[A] ruling against Downs [in arbitration] would not be imputed to Nixon Peabody." (3 RA 718.)

3. Both Downs and Nixon Peabody conceded the interrelatedness of the issues and the risk of inconsistent factual determinations.

Given the overlap, it's not surprising that Downs and Nixon Peabody both conceded the possibility of inconsistent results.

Downs. In his petition to compel arbitration, Downs argued that "[e]ach of Rice and Day's causes of action against Downs" must be ordered to arbitration. (1 RA 36-38.) He then argued that the remaining litigation—HPD's claims against Downs and Rice and Day's claims against Nixon Peabody—should be stayed because "the remaining claims are not independent but in fact contain overlapping issues" that pose a "risk of inconsistent results." (1 RA 38.) In particular, Downs told the trial court that the "claims against Nixon Peabody (*i.e.*, only the Second and Fourth Causes of Action) are based on services the firm provided, through Downs as well as other attorneys" and that they present the same issues that would be resolved in the arbitration of the claims against Downs. (1 RA 39.) Downs' petition failed to address section 1281.2(c) and instead argued that the overlap required the court to stay the litigation. (1 RA 38.)

In reply to Rice and Nixon Peabody's express reliance on 1281.2(c) (pp. 20-21, *ante*), Downs did not disagree about the application of that statute. More importantly, he did not attempt to walk back his earlier concession that there was a "possibility" of inconsistent rulings—the statutory standard. Instead, he argued that "granting the motion to compel

arbitration and staying this proceeding is *not likely* to result in conflicting or inconsistent results." (3 RA 715, italics added, capitalization normalized.) Not only did he change the test, which requires only a "possibility" rather than a likelihood of inconsistent factual rulings. He also improperly attempted to transform a review of allegations into a mini-trial on the merits:

- He argued that he would probably prevail in arbitration because his firms never represented Rice and Day and never acted inappropriately. (3 RA 710-713, 716.) In support of this contention, and without mentioning the opinion letters, he submitted evidence that he asserted "dispositively" disproved the merits of Rice and Day's claims. (See 3 RA 716.)
- He argued that if he were to prevail in arbitration, Rice and Day would be precluded from making the same claims against Nixon Peabody. (3 RA 716-718.) Under his vision, because the arbitrator would rule in his favor, the arbitration was "likely to resolve all disputes" and "render the litigation unnecessary." (3 RA 717.)

(*Abaya*, *supra*, 189 Cal.App.4th at pp. 1498-1499 [section 1281.2(c) contemplates summary proceeding that does not entail consideration of merits].)

Even so, Downs' reply brief tacitly conceded that there was a "possibility" of inconsistent results on the many common issues if he lost

the arbitration. In his words, "[w]hile an Arbitrator's ruling in favor of Downs on [the fiduciary duty] claim would effectively preclude liability of Nixon Peabody on the same claim, a ruling against Downs would not be imputed to Nixon Peabody." (3 RA 718.)

Nixon Peabody. Nixon Peabody went even further. It partially opposed Downs' petition to compel arbitration, invoking section 1281.2(c) because of a "possibility of conflicting rulings between the arbitration with Downs and litigation with Nixon Peabody" on the overlapping fiduciary duty claims. (2 RA 511, 513-515.) Because this "distinct possibility" was so strong, Nixon Peabody urged the court that it "should use its discretion afforded by Code of Civil Procedure section 1281.2(c) to deny arbitration" as to the malpractice and fiduciary duty claims. (*Ibid.*)

In a separate filing, Nixon Peabody argued that there was no possibility of inconsistent rulings with respect to a *different* set of claims—breach of contract and unjust enrichment arising from Downs and Nixon Peabody's billing for Downs' legal services. (3 RA 699-701 [Nixon Peabody's opposition to Rice and Day's stay motion].) But as Nixon Peabody's two simultaneous briefs made clear, the arguable overlap in Claims 3 and 4 (fee entitlement) was entirely separate from the conceded overlap in Claims 1 and 2 (fiduciary duty). (See 1 RA 9-17.)

C. The Trial Court's Analysis Erroneously Failed To Address The Indisputable, And Conceded, Overlap That Created A Possibility Of Inconsistent Rulings.

The trial court nevertheless concluded that "there is no basis to deny arbitration" because of possible conflicting rulings. (3 RA 747-748.) It reached that conclusion by ignoring the overlap in the fiduciary duty claims. Instead, it considered only Rice and Day's argument about overlap as to the *other* set of claims—breach of contract and unjust enrichment related to defendants' right to bill for Downs' legal services. (3 RA 746-748.)

Rice and Day repeatedly asked the trial court to consider the overlap regarding *both* the fiduciary duty claims *and* the claims concerning defendants' right to charge for Downs' services. (3 RA 727-728; 2 RA 377-379, 396-398.) Their section 1281.2(c) argument exhaustingly detailed the overlap in fiduciary duty claims. (2 RA 377-379, 396-398.) Their reply brief in support of their motion to stay likewise squarely addressed the potential for inconsistent rulings regarding claims for "malpractice" and breach of "fiduciary duties"—as well as for the billing claims—explaining that there was a possibility of inconsistent rulings regarding whether "Downs (acting at times as a Nixon Peabody attorney) improperly advised, billed, or hindered the business of HPD and its members, thereby causing harm to the individual Plaintiffs . . . ." (3 RA 727-728.)

Nixon Peabody similarly urged the court to deny arbitration of the fiduciary duty claims. (2 RA 511, 513-515.) It only disagreed with Rice and Day regarding the possibility of inconsistent rulings on the separate claims regarding defendants' right to charge for Downs' legal services. (3 RA 699-701.)

But the trial court never addressed the undisputed overlap in the fiduciary duty claims. Its order is clear: It considered *only* the asserted overlap on the claims concerning defendants' right to charge for Downs' services. As the court put it, "Plaintiff asserts that there is a risk of conflicting rulings because there is a dispute as to Defendant Downs' entitlement to be paid for his legal services." (3 RA 746.) The court disagreed with *that* argument, because the operating agreement's compensation provision only bound Downs and the other HPD members—not Nixon Peabody. (3 RA 747.) The "issue of Defendant Downs' remuneration under the Operating Agreement is an internal conflict between the members of Plaintiff Highland Properties Development, LLC." (*Ibid.*) The court explained that "Nixon Peabody, LLC is an outside party" and thus, the arbitration issue of Downs' right to compensation is "irrelevant to the third parties, Highland Properties Construction, Inc. and Defendant Nixon Peabody . . . ." (*Ibid.*)

Based on that limited assessment, the trial court concluded that section 1281.2(c) was not triggered. (3 RA 747-748.) But, as demonstrated above, the complete analysis plainly reveals the possibility of conflicting rulings. That risk was not just conceded but undeniable.

D. The Trial Court's Section 1281.2(c) Error Requires Reversal Of The Order Compelling Arbitration.

The trial court's failure to exercise its discretion under section 1281.2(c) requires this Court to vacate the order compelling arbitration. (*Orabuena, supra*, 116 Cal.App.4th at p. 99.) And because that leaves no basis for the arbitration of Rice and Day's claims, the Court must also set aside the dismissal of those claims, whether with or without prejudice.

The only real question is whether this Court should deny arbitration outright or instead remand so that the trial court can exercise discretion over that issue. Either way, the result will be new proceedings in which the parties have an opportunity to actually present the merits of their dispute—rather than allowing Downs and Nixon Peabody to avoid the claims by engaging in a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their fiduciary duty claims (16 AA 4420).

1. The proper remedy is reversal with directions to deny enforcement of the arbitration agreement.

This is not a case with a single, narrow overlapping issue. The claims against Downs and Nixon Peabody are inextricably intertwined in a mass of overlapping issues of fact and law. Although courts have discretion regarding how to act once section 1281.2(c) is triggered (p. 57, *ante*), here that discretion could have been permissibly exercised in only one way.

It isn't surprising that the Legislature vested courts with discretion. The extent and significance of the common issues necessarily informs the correct approach in each case. A litigant can invoke the statute based on a single, minor factual issue common between two otherwise distinctly separate cases. Such a slight overlap might create some small duplication of efforts and some small chance of inconsistent rulings. But in all likelihood, it would not so impact section 1281.2(c)'s policy concerns as to trump the strong public policy favoring arbitration.

This case, however, presents no occasion for pause or debate. The twin policy concerns announced by our Supreme Court are at their maximum.

First, the fiduciary duty claims against Downs and Nixon Peabody are numerous. Rice and Day allege a large number of distinct acts during multiple periods, and each constituted a separate breach of the fiduciary duty. (1 RA 12-14.)

Second, the number of common issues is overwhelming. There is complete overlap as to all of the various alleged acts, with the exception of Downs' misconduct before he became a Nixon Peabody partner. That means that there is complete overlap as to nearly every factual and legal sub-issue that may arise.

Third, the extensive common issues are the very heart of the complaint and they address significant issues of public policy concerning an attorney's duties to his clients, particularly when that attorney engages in

business transactions with his clients. Business dealings between attorneys and clients are "always scrutinized by courts with jealous care, and are set aside at the mere insistence of the client" unless the attorney satisfies his burden of proof to "show that the dealing was fair and just, and that the client was fully advised." (*Beery v. State Bar* (1987) 43 Cal.3d 802, 812-813; see also *Passante v. McWilliam* (1997) 53 Cal.App.4th 1240, 1248 ["In a business transaction with a client, notes our Supreme Court, a lawyer is obligated to give 'his client all that reasonable advice against himself that he would have given him against a third person"].) Indeed, Downs' own counsel described the magnitude of Rice and Day's claims as "enormous." (7 AA 1811:8-9.)

As one trial court put it in denying arbitration under section 1281.2(c), "'the issues are too inextricably mixed between the arbitration and the civil action, that there is no reason to conduct the arbitration as well as the civil action.'" (*Lindemann v. Hume, supra,* 204 Cal.App.4th at p. 568 [quoting trial court's reason for denying arbitration and finding no abuse of discretion].) In *Lindemann* the overlap was far less extensive. There, the plaintiff alleged numerous construction defects against the developer, in large part related to the construction of a foundation. (*Id.* at pp. 562-563.) The arbitrable claims against the seller of the real property involved only the failure to disclose one of those alleged defects, a drainage problem, that was allegedly known to the seller. (*Id.* at pp. 563, 566.) Nonetheless, because a threshold issue in both claims was "whether there was a problem with the construction of the property in the first instance,"

the trial court determined that the cases were inextricably mixed. (*Id.* at p. 563.) Here, the degree and significance of the overlap is far greater. The high number of common issues and the complete interdependence of the arbitration and litigation make the possibility of inconsistent rulings extremely high and make the substantial duplication of efforts intolerable.

2. At very least, the court must reverse so that the trial court can exercise its discretion.

In any event, reversal is necessary to cure the trial court's failure to exercise its discretion under section 1281.2(c) because of its erroneous belief that there were no common issues creating a possibility of inconsistent results and thus "no basis to deny arbitration." (3 RA 747-748.) A trial court's failure to exercise discretion is an abuse of discretion, even when based on a mistaken belief it lacked discretion. (*Orabuena, supra*, 116 Cal.App.4th at p. 99; *In re Marriage of Rosenfeld and Gross* (2014) 225 Cal.App.4th 478, 485.)

As we have demonstrated, it is at least reasonably probable that the trial court would have reached a different conclusion had it considered the extensively intertwined nature of the fiduciary claims. Moreover, it is inherently prejudicial to be forced to arbitrate a claim that one never agreed to arbitrate—to be forced to surrender the protections of strict adherence to the law, rules of evidence and judicial oversight. Likewise, it is prejudicial to waste valuable resources by being forced into duplicative arbitration (against Downs) and litigation (against Nixon Peabody) of the same issues.

Fortunately, that wastefulness has thus far not occurred because Rice and Day's claims have never been tried in any forum—the claims against Downs were dismissed from arbitration before the arbitration hearing, and the claims against Nixon Peabody remain pending in the civil case.

RESPONDENT'S BRIEF

STANDARDS OF REVIEW

Vacatur. The Court reviews de novo the trial court's decision to vacate the arbitration award. (*SWAB Financial v. E*Trade Securities* (2007) 150 Cal.App.4th 1181, 1196 (*SWAB Financial*).) However, the trial court's detailed factual findings on disputed issues are reviewed for substantial evidence. (*Ibid.*)

Fee award. Downs' challenge to the amount of attorneys' fees award is reviewed for abuse of discretion. (*Cruz v. Ayromloo* (2007) 155 Cal.App.4th 1270, 1274.)

ARGUMENT

I. REVERSAL OF THE ORDER COMPELLING ARBITRATION WILL RENDER DOWNS' APPEAL MOOT.

The cross-appellant's opening brief shows that the order compelling arbitration must be reversed. That result would mean that Rice and Day's claims should never have been part of the arbitration. In turn, this would mean that the dismissal of those claims from arbitration, whether with or without prejudice, would never have been an issue, and the trial court would never have been called upon to either confirm or vacate the dismissal order. That would leave nothing for Downs' appeal to attack.

This is the very essence of mootness—an issue as to which there is no longer any need for a decision. (*MHC Operating Ltd. Partnership v. City of San Jose* (2003) 106 Cal.App.4th 204, 214 ["A case is moot when

the decision of the reviewing court 'can have no practical impact or provide the parties effectual relief.'"].) The court should therefore dismiss Downs' appeal on that basis. (*Ibid.*)

II. ASSUMING ARGUENDO THAT THIS COURT NEEDS TO REACH THE ISSUE, IT SHOULD AFFIRM: THE TRIAL COURT PROPERLY VACATED THE WITH-PREJUDICE DISMISSAL OF RICE AND DAY'S CLAIMS.

Downs devotes most of his brief to demonstrating something that isn't in dispute: that trial courts can only vacate an arbitration award on the grounds enumerated in Code of Civil Procedure section 1286.2. He completely ignores an argument that he knew Rice would raise, because it was the centerpiece of Rice's opposition to Downs' writ petition: Whether the trial court's detailed factual findings require affirmance on alternative grounds that are firmly based in section 1286.2. (See AOB 32.) He likewise ignores those factual findings. Instead, he says that he "will wait to see if Rice and Day raise" the same issue in opposition to Downs' appeal. (AOB 32.) Depending on Downs' reply arguments, Rice may need to seek leave to file a sur-reply.

A. The Award Must Be Vacated Because It Was Procured By Undue Means.

1. Section 1286.2 requires vacatur when the court determines that the award was procured by undue means.

Section 1286.2 provides that the court "shall" vacate the award if it was "procured by corruption, fraud or other *undue means.*" (Code Civ. Proc., § 1286.2, subd. (a)(1), italics added.) Here, the trial court's factual findings amply demonstrate that the dismissal was procured by undue means. As the trial court put it, Downs and his firm engaged in a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their claims. (16 AA 4420.) Whatever non-statutory label the trial court attached, its factual findings don't just support vacating the dismissal with prejudice—they mandate it.

a. Governing law.

Our courts define undue means as "'behavior that is immoral if not illegal'" or conduct that is "'not proper.'" (*Pour Le Bebe, Inc. v. Guess? Inc.* (2003) 112 Cal.App.4th 810, 831 (*Pour Le Bebe*), quoting *A.G. Edwards & Sons, Inc. v. McCollough* (9th Cir. 1992) 967 F.2d 1401, 1403-1404 and Black's Law Dictionary 1679 (Rev. 4th ed. 1968).) Although the term does not include all conduct that "in any way seem[s] unfair," it is clear that a party utilizes undue means when he engages in procedural maneuverings that deny the other party the opportunity to present his case

during the actual arbitration hearing. (*Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 827, 832-833.)

In contrast, for example, a party does not employ undue means merely by offering a meritless defense. (*Id.* at pp. 831-832.) For one thing, offering a meritless defense "'carries no connotation of wrongfulness or immorality.'" (*Id.* at p. 831, quoting *A.G. Edwards & Sons, Inc., supra,* 967 F.2d at pp. 1403-1404.) Such conduct, "'however unfortunate, is part and parcel of the business of litigation'"; it occurs "'with such frequency'" that courts would vacate awards "'regularly'" if the assertion of a meritless defense constituted undue means. (*Ibid.*) More importantly, "[w]here meritless legal arguments are raised in an arbitration, the opposing party has a full and fair opportunity to contest them . . . ." (*Id.* at p. 832.)

On the other hand, California courts have held that parties utilize undue means when they:

1. Raise a new argument in a post-hearing brief, depriving the other party of the opportunity to present evidence to the arbitrator (*Pacific Crown Distributors v. Brotherhood of Teamsters* (1986) 183 Cal.App.3d 1138, 1146; see *Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 832-833);

2. Contact the arbitrator ex parte through a post-arbitration letter brief, preventing the other party from presenting rebuttal argument on a legal issue (*Maaso v. Signer* (2012) 203 Cal.App.4th 362, 372); or

3. Are represented by an attorney who should have been conflicted out of the case because the attorney previously represented and possessed confidential information about the opposing party (*Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 815-816, 825, 833 [finding undue means, but affirming denial of vacatur for lack of nexus between undue means and award, see p. 78, *post*]).

In each case, the key criterion was that one side's wrongful conduct deprived the other of an opportunity for a fair hearing on the merits. (*Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 832-833.)

California goes further in protecting a party's fair-hearing opportunity than do some federal courts applying federal law. For instance, under the Ninth Circuit's interpretation of federal law, if the undue means is "not only discoverable, but discovered and brought to the attention of the arbitrators, a disappointed party will not be given a second bite at the apple." (*A.G. Edwards & Sons, Inc., supra,* 967 F.2d at p. 1404; see *Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 831-832 [explaining rule].) California courts have explicitly rejected that rule: A party "who did not receive a hearty 'first bite' could not be precluded from having a 'second bite.'" (*Pour Le Bebe, supra,* 112 Cal.App.4th at p. 832.) To do otherwise would "compromise the basic due process rights of [a party] as codified in Code of Civil Procedure section 1282.2, subdivision (d)." (*Pacific Crown Distributors, supra,* 183 Cal.App.3d at pp. 1148-1149.) Accordingly, California courts have held that a prevailing party who utilized undue means could not hide behind the fact that the arbitrator explicitly or

implicitly saw no problem with the alleged misconduct, if that deprived the losing party of the "'opportunity to rebut his opponent's claims *at the arbitration hearing*.'" (*Pour Le Bebe*, *supra*, 112 Cal.App.4th at pp. 832-833 [when alleged undue means was the use of an attorney who was conflicted out of the case, court could review the issue even though the arbitrators refused to disqualify the attorney in a "summary" proceeding before the hearing]; e.g., *Pacific Crown Distributors*, *supra*, 183 Cal.App.3d at pp. 1146-1149 [reviewing appropriateness of party raising an issue in post-hearing brief although arbitrator saw no problem and relied on that brief].)

There is one other requirement: To vacate an award, there must also be a "nexus between the award and the alleged undue means used to attain it." (*Pour Le Bebe*, *supra*, 112 Cal.App.4th at pp. 833-834.) The rule stems from concerns that "a court should not presume that [the undue means] had an impact on the arbitrators." (*Id.* at p. 833.) For instance, in one example discussed in *Pour Le Bebe*, the party seeking vacatur asserted that the prevailing party had intimidated an expert witness. (*Ibid.*) But because the "aggrieved party had the opportunity to present the testimony of other expert witnesses and the threatened expert agreed to nevertheless testify, the court could not say that the alleged misconduct had such a 'substantial or pervasive' impact on the 'award arrived at by the arbitrators after lengthy hearings and the presentation of substantial evidence by both sides.'" (*Ibid.*)

b. The trial court's factual findings, which are binding on this Court, compel the conclusion that the award was procured by undue means.

Downs and Nixon Peabody's "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their claims more than suffices to establish the type of undue means that requires courts to vacate an arbitration award. Although the trial court sought to address this unfairness through its inherent powers, the statutory grounds for vacatur clearly apply.

The trial court's factual findings are binding. (*Environmental Law Foundation v. Beech-Nut Nutrition Corp.* (2015) 235 Cal.App.4th 307, 322 [appellate court is bound by factual findings supported by substantial evidence]; *SWAB Financial*, *supra*, 150 Cal.App.4th at p. 1196 [substantial evidence standard applies to trial court's factual determinations in decision to vacate an award].) Both parties presented voluminous evidence on their respective versions of what happened during discovery. (See p. 31, fn. 2, *ante*.) The trial court rejected Downs' attempt to blame Rice and Day's counsel for not acting diligently, calling that characterization "misleading." (16 AA 4419.) Instead, the court credited Rice and Day's evidence, saying that it "persuasively" demonstrated that Downs and Nixon Peabody engaged in "a coordinated campaign to delay and deflect." (16 AA 4420.)

That "campaign" easily satisfies the standard for undue means:

1. Downs and Nixon Peabody went to extraordinary lengths to foreclose Rice and Day's ability to obtain discovery and thus their ability to present their claims in arbitration. Embarking on such a thorough and "coordinated campaign" carries at least as strong of a "connotation of wrongfulness or immorality" as raising an issue in a post-hearing brief. (*Pacific Crown Distributors, supra,* 183 Cal.App.3d at p. 1146; *Pour Le Bebe, supra,* 112 Cal.App.4th at pp. 831-833.) Both seek to—and do—prevent the other party from being able to fully present his case.

Downs' campaign was particularly egregious. He refused to comply with most of Rice and Day's document requests, claiming that the requested documents—including his own emails—were within Nixon Peabody's possession and that he could not provide them despite being a partner in that firm. (See p. 24, *ante*.) When Rice and Day then turned to Nixon Peabody, the abuses continued and intensified—including using building security to prevent service of a subpoena. (Pp. 24-25, *ante*.) The arbitrator ultimately ordered Downs to accept service of the Nixon Peabody subpoena and, if Nixon Peabody still resisted, to arrange to escort the process server through security and to a person authorized to accept service. (12 AA 3282.)

And when Nixon Peabody finally provided responses—the Friday a few days before Christmas, just weeks before the hearing, and after the

completion of depositions—the production was both unwieldy and incomplete. (16 AA 4421; p. 26, *ante*.)

This "coordinated campaign" is not simply "part and parcel of the business of litigation" or something that occurs with "such frequency" that it might result in courts "regularly" vacating awards. (*Pour Le Bebe*, *supra*, 112 Cal.App.4th at p. 831.) It is nothing like the assertion of a meritless claim that both sides could dispute at a hearing on the merits. (*Ibid.*) It was an extraordinary series of tactics that was especially wrongful given that Downs and his firm are officers of the court and, as many documents demonstrate, Downs and his firm did in fact represent Rice and Day individually and owed them fiduciary duties. (See pp. 29-30, 62, *ante*.)

2. Downs and Nixon Peabody's "coordinated campaign" deprived Rice and Day of a full and fair opportunity to present the merits of his case in arbitration. (*Pour Le Bebe*, *supra*, 112 Cal.App.4th at pp. 831-833.) As the trial court found, that was the very purpose and effect of their extraordinary efforts. Without the relevant documents, Rice and Day could not take the next steps in discovery, including depositions regarding the documents. (Pp. 25-26, *ante*.) Without the relevant information, Rice and Day were handicapped in the arbitration hearing and less likely, if not entirely unable, to carry their burden of proof. Deprived of any ability to prosecute their claims, Rice and Day ultimately tried to preserve their rights by dismissing their claims without prejudice. (Pp. 26-27, *ante*.)

3. A nexus unquestionably existed between the undue means and the arbitration award (*Pour Le Bebe, supra*, 112 Cal.App.4th at pp. 833-834) as the trial court easily found (16 AA 4423).

This is not an instance where the undue means had no substantial effect or where the arbitrator might have decided the claim based on some unrelated issue. (See p. 78, *ante*.) Rice and Day dismissed their claims without prejudice because their efforts to procure discovery documents had been frustrated. Downs then capitalized on the situation by having the arbitrator convert the dismissal without prejudice into a dismissal with prejudice.

Indeed, the trial court highlighted Downs' argument to the arbitrator as proof of the nexus. (16 AA 4423.) Downs relied on Rice and Day's inability to present the very evidence that he and Nixon Peabody had kept Rice and Day from obtaining as the basis for dismissal with prejudice:

> He argued that Rice and Day have been unable to "state[] any facts to support their central allegation" despite the passage of nearly a year since the inception of the arbitration and that Downs "disputes the notion he or any law firm he was with personally represented Rice or Day." (2 AA 515, 517, fn. 3.)

That's not just a nexus. It is unquestionable cause and effect.

c. Downs' contrary arguments are meritless.

(1) Downs' substantive arguments are meritless.

We assume that Downs will respond with arguments similar to those he offered in his reply in support of his writ petition. None has any merit.

First, Downs seems to believe that the trial court rejected the undue means argument because it "found 'no clear and convincing evidence of fraud . . . .'" (17 AA 4705, citing court order found at 16 AA 4417, 4421.) Not so. This finding addressed whether Rice and Day had shown *perjury* in Downs' repeated denials that he and his firms ever represented Rice and Day individually. (16 AA 4414-4421.) The court felt unable to find perjury because there was no clear and convincing evidence that Downs had "willfully" testified untruthfully. (16 AA 4417.) The trial court's perjury analysis also applied the Ninth Circuit's test for "fraud," including whether the perjury was discoverable. (16 AA 4411, 4414, 4417-4421.) But in California, that test does not apply to "undue means" that interfere with a party's opportunity to receive a full and fair hearing. (See pp. 77-78, *ante*; *Pour Le Bebe*, *supra*, 112 Cal.App.4th at pp. 831-832 [explaining and distinguishing Ninth Circuit's three-part test from California undue means analysis].)

Second, Downs argued that there could not have been any undue means because, according to him, the trial court found that all of the evidence that he and Nixon Peabody wrongfully withheld was "in Rice's

possession before the arbitration hearing." (17 AA 4704-4705.) Indeed, Downs thinks that this is the key to distinguishing *Pacific Crown Distributors*, *supra*. (*Ibid*.) Again, not so.

The trial court found *only* that the "*Opinion Letters* were available to counsel before counsel moved to dismiss the malpractice claim, without prejudice." (16 AA 4421, italics added.) Those opinion letters could help prove one sub-issue in the case—whether Downs and his firms represented Rice and Day individually. (See pp. 29-30.) But Downs and Nixon Peabody engaged in a "coordinated campaign to delay and deflect" *all* discovery on a *broad range* of issues—including discovery of evidence that would help prove that Downs engaged in conduct that breached his duty. (See 12 AA 3174-3183 [requests to Downs], 3209-3219 [requests to Nixon Peabody].) It was that *generalized* denial of discovery that constituted the undue means.

For instance, Rice and Day sought "all communications relating to the performance of legal services for HPD, HPA, or HPC between you and any attorney, paralegal or secretary employed or contracted with your law firm," all documents relating to the formation of the parties' businesses, and all documents relating to Downs and his firms' efforts to comply with Rule 3-300. (12 AA 3182-3183, capitalization normalized.) The breadth of the affected discovery is evidenced by the production that Rice and Day finally received from Nixon Peabody after dismissing their claims without prejudice—20,000 emails and nearly 34,000 other documents. (7 AA 1875 at ¶ 8; 12 AA 3171; 16 AA 4421.) The trial court found that even this

production did not completely respond to Rice and Day's requests. (16 AA 4421; see 12 AA 3292.) So, the delayed and denied discovery was certainly not just a matter of 23 opinion letters.

As the trial court found, the reason Rice and Day dismissed their claims "was that Plaintiffs' efforts to procure discovery documents had been frustrated" through a coordinated campaign by Downs and his firm. (16 AA 4421.) It was global delay and denial of discovery that constituted the undue means. That does not change merely because, unbeknownst to them, Rice and Day already had access to some evidence—the opinion letters—that were relevant to the sub-issue of whether Downs and his firm ever represented Rice and Day individually.

Third, Downs will presumably continue to argue that *Pour Le Bebe*, *supra*, 112 Cal.App.4th 810, warned against overly broad interpretations of undue means and that the term does not extend to anything that might be described as "unfair." (17 AA 4704.) That is true. But, as demonstrated above, *Pour Le Bebe* also made clear that undue means connotes wrongfulness or immorality that deprives the other party of a full and fair opportunity to present the merits of his case during the actual arbitration hearing. (Pp. 75-77, *ante*.) That is precisely what happened here—and by an officer of the court.

Fourth, Downs may argue that questioning the fairness of Downs and Nixon Peabody's conduct or the resulting dismissal of Rice and Day's claims intrudes on the arbitrator's decision-making power. (Cf. AOB 30-

32.) But under California's undue-means review, a party "who did not receive a hearty 'first bite [at the apple]' could not be precluded from having a 'second bite.'" (*Pour Le Bebe*, *supra*, 112 Cal.app.4th at p. 832.) Just as in *Pour Le Bebe*, "it cannot be said" that Rice and Day had an opportunity to "reveal the alleged undue means *at the arbitration hearing*"; a "summary" proceeding in advance of the hearing is insufficient. (*Pour Le Bebe, supra,* 112 Cal.App.4th at p. 833, italics in original.)

In any event, it is for the courts to determine whether the alleged conduct included wrongfulness or immorality that denied a fair and full opportunity to present the merits of the case. (See pp. 75-78, *ante*.) Otherwise, undue means review would be meaningless.

Fifth, Downs may argue that Rice and Day should have asked the arbitrator to continue the hearing. That might have been appropriate under normal circumstances where a party needs more time. But here, Rice and Day had repeatedly tried to obtain discovery and Downs and Nixon Peabody had repeatedly gone to extreme lengths to frustrate those efforts. Discovery was not forthcoming even after the arbitrator ordered various means to force Downs to get Nixon Peabody to comply. Having engaged in a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute his claims, Downs can hardly complain that it would have been better if Rice and Day had sought a continuance rather than a dismissal without prejudice. A party should not be allowed to profit because the plaintiff responded to undue means by choosing dismissal without prejudice rather than seeking a continuance. That is especially so for

Downs—who, as an officer of the court and Rice and Day's fiduciary, is held to higher standards.

(2) Downs' procedural arguments are meritless.

Waiver. It is not clear whether Downs thinks that the undue means argument is "procedurally barred" for having not been raised below. (AOB 32; see also AOB 25, fn. 5, 33, fn. 7.) His opening brief says that a different issue—unconscionability of the award—was not raised and is thus barred. (AOB 32.) In fact, with respect to the argument that discovery delays constituted undue means, Downs' reply in support of his writ petition stated that "Rice argued those same issues to Respondent Court"—meaning that the issue is not new at all. (17 AA 4704-4705.) In any event, Rice's undue means argument is not barred.

It is elementary that appellate courts must affirm an order if it is "right upon any theory . . . regardless of the considerations which may have moved the trial court to its conclusion." (*Transamerica Ins. Co. v. Tab Transportation, Inc.* (1995) 12 Cal.4th 389, 399, fn. 4; see also *In re Conservatorship of Estate of Davidson* (2003) 113 Cal.App.4th 1035, 1056, disapproved on other grounds by *Bernard v. Foley* (2006) 39 Cal.4th 794, 816, fn. 14 [appellate court must affirm if trial court's order is right for any reason, regardless of the correctness of the grounds upon which the lower court reached its conclusion].)

Here, the trial court found *as a factual matter* that Downs and his firm engaged in a "coordinated campaign to delay and deflect" Rice and Day's ability to prosecute their claims, thwarting discovery at every turn. (16 AA 4418-4420.) It further found *as a factual matter* that it was this conduct—and Downs' resulting argument that Rice and Day lacked evidence to prove their case—that resulted in the conversion of the dismissal of Rice and Day's claims into a with-prejudice dismissal. (16 AA 4421, 4423.) Downs has not suggested that these findings are not supported by substantial evidence—indeed, he doesn't even acknowledge their existence. Nor would there be any basis for such a claim.

The trial court ultimately recognized the fundamental unfairness of the arbitrator's conversion of the dismissal into a dismissal with prejudice and that "justice demands" that the award be vacated in that regard. (16 AA 4428-4429.) The trial court labeled its vacatur order a non-statutory exercise of the court's inherent powers. (*Ibid.*) But, as we have shown, that is the wrong label: While justice and fairness *do* demand vacatur, the statutory scheme refers to this circumstance as an award procured by undue means. In light of the trial court's factual findings, this Court must affirm because the order is correct, albeit on a different ground than the trial court applied.

The waiver case that Downs cites, *Delaney v. Dahl* (2002) 99 Cal.App.4th 647, 660, is not contrary. (AOB 32-33, fn. 7.) In *Delaney*, the trial court confirmed an arbitration award and denied a petition to vacate. (99 Cal.App.4th at p. 654.) At oral argument in the Court of

Appeal, the appellant raised an entirely new basis for seeking *reversal* of the trial court's order. The court rejected the argument on its merits, and also noted that the newly-raised issue could be deemed waived. (*Id.* at p. 660.)

Those aren't our circumstances. Rice does not seek to *reverse* an order based on a new theory. He seeks *affirmance* on the basis of a long-established principle of appellate review—and in any case, the issue presented is not truly new. Rice and Day sought to vacate the award based on "fraudulent and undue means," asserting section 1286.2, subdivision (a)(1)—the very same subdivision on which he now relies. (See 5 AA 1293.) The issue has always been whether the arbitrator permissibly converted Rice and Day's dismissal without prejudice into a dismissal with prejudice. And the factual issues presented are identical—the parties' competing views regarding whether Downs and his firm stonewalled Rice and Day in the discovery process. (See p. 31, fn. 2, *ante*.) For instance, below, Rice and Day devoted more than four pages of one of their briefs to the argument that "the incomplete Nixon production was tactically timed to avoid the use of the documents contained therein." (7 AA 1855-1859, capitalization normalized.) That is presumably why, as to the undue means argument made in opposition to Downs' writ petition and now on appeal, Downs has said that "Rice argued those same issues to Respondent Court." (17 AA 4705.)

Another portion of Downs' opening brief seems to suggest that the statutory scheme might limit review. In a footnote, Downs says that a "trial

court cannot act *sua sponte* to vacate, correct, or confirm an award; such relief can be granted only if a timely petition or response is filed by one of the parties to the arbitration." (AOB 25, fn. 5, citing Code Civ. Proc., § 1286.8.) But there is no question that Rice and Day timely filed and served a petition to vacate (see 5 AA 1276 [Downs' concession]), and the statutes impose no restrictions on the *grounds* on which a court can vacate an award. Indeed, they don't even prohibit a court from vacating an award when the petition seeks correction rather than vacatur. (Code Civ. Proc., § 1286.4, subds. (a)-(b) [court may not vacate an award unless either a petition to vacate "or" a petition to correct has been duly served and filed].) In those circumstances, a court can vacate an award "on its own motion," which can only mean that the trial court can sua sponte raise a ground to vacate the award once vested with jurisdiction. (Code Civ. Proc., § 1286.4, subd. (b)(2).)

* * * * *

The Court need not dwell on the trial court's "inherent powers" label. Whatever label the trial court ascribed, this Court must affirm on any ground supported by the record. Here, the trial court's factual findings and concerns require vacatur based on undue means—Downs procured the dismissal of Rice and Day's claims with prejudice by using a coordinated campaign to deny Rice and Day the opportunity to fully and fairly present their claims on the merits.

B. In The Alternative, The Award Must Be Vacated Because It Imposed A Remedy Prohibited By The Parties' Arbitration Agreement.

1. Because the parties limited the arbitrator to remedies available in court, the arbitrator had no power to convert the dismissal without prejudice to a dismissal with prejudice.

"'The powers of an arbitrator derive from, and are limited by, the agreement to arbitrate.'" (*Gueyffier v. Ann Summers, Ltd.* (2008) 43 Cal.4th 1179, 1185, quoting *Advanced Micro Devices, Inc. v. Intel Corp.* (1994) 9 Cal.4th 362, 375.) An arbitrator exceeds her powers when she acts in a manner not authorized by contract or awards a remedy "expressly forbidden by the arbitration agreement." (*O'Flaherty v. Belgum* (2004) 115 Cal.App.4th 1044, 1056, 1061 (*O'Flaherty*).) When an arbitrator exceeds her powers, the court "shall" vacate the award. (*Id.* at p. 1055; Code Civ. Proc., § 1286.2, subd. (a)(4).)

Here, the arbitration clause states that "[t]he arbitrator shall not have any power to . . . grant any remedy which is . . . not available in a court of law." (1 RA 74-75 [original operating agreement], 110-111 [amended operating agreement], italics added.) This language is identical to the contractual limitation considered in *O'Flaherty*. (115 Cal.App.4th at pp. 1049, 1061.) It, to some extent, renders normal concerns about "limitations on judicial power over arbitration awards . . . not applicable." (*Id.* at p. 1061.) When parties limit an arbitrator's remedial powers to those

available in courts, California courts are required to examine the law to determine whether a court would in fact have the power to grant the remedy the arbitrator awarded. (*Id.* at pp. 1058-1061.)

For instance, in *O'Flaherty*, the claimant and respondents were partners in a law firm from which the respondents withdrew. (*Id.* at pp. 1048-1050.) The arbitrator decided that the withdrawing partners were liable for breach of contract, breach of fiduciary duty and conversion. (*Id.* at pp. 1051-1052.) He ruled that they had forfeited all rights under the partnership agreement, including forfeiture of their partnership accounts. (*Id.* at pp. 1051, 1056.) The trial court confirmed the award, but the Court of Appeal reversed. It explained that case law does not permit courts to award a forfeiture of a capital account. (*Id.* at pp. 1057-1059.) By providing a remedy inconsistent with the contractual limitation on awarding a remedy "not available in a court of law, the arbitrator in effect awarded 'a remedy expressly forbidden by the arbitration agreement.'" (*Id* at p. 1061.) That excess of power, required vacatur. (*Id.* at p. 1064.)

That same analysis applies here.

First, dismissal with prejudice has been repeatedly described as a "remedy" for various types of conduct, including the failure to prosecute an arbitration claim with reasonable diligence. (E.g., *Brock v. Kaiser Foundation Hosp.* (1992) 10 Cal.App.4th 1790, 1808.) It is "the functional equivalent of an award against the claimants" regardless of whether it is labeled a sanction or otherwise. (*Ibid.*) Downs' opening brief concedes

that an arbitrator's dismissal of a claim with prejudice constitutes a remedy; he only argues that "dismissal with prejudice is indisputably a 'remedy . . . available in a court of law.'" (AOB 35, ellipses in original.)

Second, courts have no power to convert a voluntary pre-trial dismissal without prejudice into a dismissal with prejudice over the plaintiff's objections. Plaintiffs have an absolute right to dismiss their claims without prejudice prior to commencement of trial. (E.g., Code Civ. Proc., § 581, subd. (c); *Kurwa v. Kislinger* (2013) 57 Cal.4th 1097, 1105 [plaintiff has "of course, the right to voluntarily dismiss a cause of action without prejudice prior to trial"]; *Gherman v. Colburn* (1971) 18 Cal.App.3d 1046, 1049 ["Prior to the actual commencement of trial, plaintiff may dismiss the action without prejudice"]; *Gogri v. Jack In The Box Inc.* (2008) 166 Cal.App.4th 255, 261 ["section 581 allows a plaintiff to voluntarily dismiss, with or without prejudice, all or any part of an action before the 'actual commencement of trial'"].) Courts have no power to revisit the voluntary dismissal and to enter an order dismissing the claim with prejudice. (*Cal-Vada Aircraft, Inc. v. Superior Court* (1986) 179 Cal.App.3d 435, 448.)

It is undisputed that Rice and Day voluntarily dismissed their claims without prejudice before the arbitration hearing actually commenced. A court would have no power to convert that to a dismissal with prejudice. By issuing a remedy inconsistent with the parties' agreed-upon limitation against awarding a remedy "not available in a court of law, the arbitrator in

effect awarded 'a remedy expressly forbidden by the arbitration agreement.'" (*O'Flaherty, supra*, 115 Cal.App.4th at p. 1061.)

2. Downs' contrary arguments are meritless.

Downs offers three contrary arguments. None has any merit.

First, Downs argues that arbitration claimants have no similar right to voluntarily dismiss their claims because "'rules of judicial procedure need not be observed' in an arbitration." (AOB 34-35, italics omitted, quoting Code Civ. Proc., § 1282.2, subd. (d).) That partial quotation isn't the law: The statute actually says that this is the case "[u]nless the arbitration agreement otherwise provides." (Code Civ. Proc., § 1282.2; see also *Sy First Family Ltd. Partnership v. Cheung* (1999) 70 Cal.App.4th 1334, 1342 ["*(u)nless the parties otherwise agree*, the rules of evidence and judicial procedure do not apply" in arbitration, italics added]; accord, *Coast Plaza, supra*, 83 Cal.App.4th at p. 690.)

If the parties had not agreed to limit the arbitrator's remedial powers to those available in court, the arbitrator's broad powers might well have included the power to convert Rice and Day's voluntary dismissal without prejudice into a dismissal with prejudice. But the parties' arbitration agreement effectively foreclosed that remedy.

Second, Downs argues that courts have the power to dismiss claims with prejudice and that the "question of when" and "under what circumstance" a court can order such a dismissal is a separate issue. (AOB 35; see 4 AA 915.) Not true. As in *O'Flaherty*, the inquiry must

be contextual. The question is not whether the remedy might be available in some other circumstance, but whether the remedy would have been available in the present case. For instance, *O'Flaherty* held that courts (and thus the arbitrator in that case) have no power to order forfeiture *in a partnership case* despite the finding of misconduct. (*O'Flaherty*, *supra*, 115 Cal.App.4th at p. 1061.) That is why the decision examined partnership law and the specific question of whether forfeiture was available in the context presented. (*Id.* at pp. 1057-1061.) Under Downs' theory, that shouldn't have mattered because courts are empowered to order forfeiture in other contexts. (E.g., *People v. Prince* (1996) 43 Cal.App.4th 1174 [civil forfeiture of drug proceeds].)

Downs' approach not only is contrary to *O'Flaherty*, but would sap the parties' agreed-upon limitation of any meaning and permit absurd results. Under his theory, the arbitrator could have awarded punitive damages in a contract case because courts are empowered to award them in other contexts. Indeed, the arbitrator could have imprisoned Rice or even ordered capital punishment because courts are empowered to impose those remedies in some cases.

It does not matter that federal courts can dismiss a complaint with prejudice for failure to plead fraud with particularity after the plaintiff fails to avail himself of the opportunity to amend his complaint. (*Vess v. Ciba-Geigy Corp. USA* (9th Cir. 2003) 317 F.3d 1097, 1102, cited at AOB 35.) Nor does it matter that federal courts can dismiss a complaint for lack of prosecution when it has been pending for years. (*Olympic Sports Products*,

Inc. v. Universal Athletic Sales Co. (9th Cir. 1985) 760 F.2d 910, cited at AOB 35.) The only question is whether a court can convert a voluntarily dismissal without prejudice into a dismissal with prejudice over the plaintiff's objections. They can't, period.[9]

Third, Downs observes that ADR Services Rule 14 permitted the arbitrator to convert a dismissal without prejudice into a dismissal with prejudice. (AOB 34-35.) Fair enough. But those general rules do not empower the arbitrator to violate the parties' specific agreement to limit the arbitrator to those remedies available in a court. In fact, as the trial court observed, "ADR Services Rules (Rule 4) themselves contemplate that when there is a conflict between the ADR Rules and applicable law, the provision of law will govern." (16 AA 4428.)

A final observation about the excess of power issue: In apparently rejecting Rice and Day's argument—"apparently" because it didn't expressly decide the issue—the trial court applied the wrong standard.

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[9] Although Downs has waived the argument on appeal (e.g., *Doe v. California Dept. of Justice* (2009) 173 Cal.App.4th 1095, 1115), below he urged that courts can "convert" a dismissal without prejudice into a dismissal with prejudice (4 AA 914-915). That argument also entirely ignored context. One of the cases he cited, *Herbert Hawkins Realtors, Inc. v. Milheiser* (1983) 140 Cal.App.3d 334, held only that after a case had been fully resolved by judicial arbitration, the losing party could not request a trial de novo and then dismiss that request without prejudice to "effectively nullif[y] the arbitrator's decision." (*Id.* at p. 337.) The other case he cited, *Wells v. Marina City Properties, Inc.* (1981) 29 Cal.3d 781, reaffirmed the general rule that a plaintiff has the right to dismiss his claim without prejudice before trial. The Court merely recognized that no such right existed after the court sustained a demurrer with leave to amend the complaint and the plaintiff failed to amend. (*Id.* at pp. 789-790.) Neither case suggests that courts are empowered to simply convert a dismissal without prejudice into a dismissal with prejudice in all contexts.

The court stated that "[t]here is no *clear and convincing evidence* that the Arbitrator exceeded her authority by dismissing the claims, with prejudice, yet, her decision is not wholly automatically supported by the ADR rules." (16 AA 4428, italics added.) But as far as our research reveals, no authority even suggests that excess of power involves a clear and convincing evidence standard. In fact, in the usual case—and certainly in this one—the question is purely legal. (See, e.g., *O'Flaherty*, *supra*, 115 Cal.App.4th 1044 [mentioning no such standard].) And as to excess of powers, Downs neither suggested that stringent standard below nor urges it on appeal. (13 AA 3735-3755; AOB 34-35.)

III. DOWNS' DUE PROCESS ARGUMENT IS IRRELEVANT AND MERITLESS.

Downs argues that the trial court denied him due process by basing the order on "inherent powers" without providing him a "meaningful opportunity to address that issue." (AOB 36-37.) That question is irrelevant since Rice doesn't seek affirmance on the basis of the trial court's inherent powers. As demonstrated above, the order must be affirmed based on undue means. That issue was certainly raised. (See p. 89, *ante*.) And Downs fully availed himself of the opportunity to present his version of what happened in discovery. Indeed, he submitted multiple declarations on the subject and tried to blame Rice and Day's arbitration counsel for not being diligent. (See pp. 26, 31, fn. 2, *ante*.) The trial court credited Rice and Day's version as persuasive and rejected Downs' argument as misleading. (16 AA 4419-4420.) Alternatively, Rice seeks affirmance

based on the remedial limits set by the parties' arbitration agreement—an argument that was raised in Rice and Day's initial petition to vacate the award. (2 AA 370-395.)

Even if it were relevant, Downs' due process argument is meritless. Downs himself acknowledges that he had an opportunity to address—and *did* address—the inherent powers issue in his written response to Rice and Day's brief. (AOB 36.) He also had more than enough time to do so: Downs filed that brief a full month after Rice and Day argued inherent powers. (7 AA 1865-1867 [Rice and Day's November 20, 2014 brief]; 14 AA 3811 [Downs' December 22, 2014 brief].) This is nothing like the primary case on which Downs relies—*Gomez v. Acquistapace* (1996) 50 Cal.App.4th 740, 743-744—where a party was denied an opportunity to confront new factual arguments that were presented just two days before a summary judgment hearing.

Downs' only complaint is that he didn't think the issue was important enough to merit more than a "limited response" and chose to focus most of his brief, for which he "had only 15 pages," on other subjects. (AOB 36.) That is not a due process violation. Indeed, Downs could have asked for additional pages to more fully address all of the issues. He didn't. He could have sought reconsideration or a new trial. He didn't. Instead, he appealed. He cannot now complain that the trial court denied him due process by not permitting additional briefing.

Besides, Downs is hardly in a position to complain about denials of due process after his "coordinated campaign" to delay and deny discovery that deprived Rice and Day of the ability to prosecute their claims.

IV. THE TRIAL COURT DID NOT ABUSE ITS DISCRETION IN LIMITING THE AMOUNT OF DOWNS' FEE AWARD: DOWNS LOST ON THE ONLY DISPUTED ISSUE PRESENTED IN THE TRIAL COURT PROCEEDING.

Downs complains that the trial court was required to award him fees and costs for *losing* on Rice and Day's petition to vacate. (AOB 37-40.) It was not, and it did not abuse its discretion in refusing to do so.

Downs sought confirmation of the entire award, which included his claims against Rice and Day. (1 AA 18-24; see p. 27, *ante*.) Rice and Day sought to vacate the award only to the extent that the arbitrator dismissed Rice and Day's claims with prejudice. (2 AA 370-374.)

On October 22, 2014, the trial court granted Downs' petition to confirm the award "except as to the arbitrator's ruling to convert the dismissal, without prejudice, to a dismissal with prejudice"—the sole disputed issue. (7 AA 1846.) That portion of the award was still under submission and was the subject of the court's order for additional briefing. (7 AA 1844-1846.) Nonetheless, at that point, the trial court granted Downs a modest amount of attorneys' fees and costs for bringing his petition to confirm. (7 AA 1846.)

After the additional briefing, the trial court agreed with Rice and Day and partially vacated the award. (16 AA 4428-4430.) Not surprisingly, the court also rejected Downs' request for more than $320,000 that he incurred in unsuccessfully opposing Rice and Day's petition to partially vacate. (16 AA 4429-4430.)

The trial court acted well within the bounds of its discretion. (See *PLCM Group, Inc. v. Drexler* (2000) 22 Cal.4th 1084, 1096 [amount of fees to be awarded is within the trial court's discretion].) The degree of a party's success impacts the reasonableness of a fee request and courts have discretion to reduce fee awards accordingly. (*Harman v. City & County of San Francisco* (2007) 158 Cal.App.4th 407, 425-426.) Downs *lost* on *the only contested issue*—the dismissal with prejudice. That was the only thing that really mattered in the trial court proceeding—the rehabilitation of fiduciary duty claims that Downs' attorney described as "enormous." (7 AA 1811:8-9.)

Downs notes that in granting vacatur, the trial court did not rely on allegations of Down's perjury or the contractual limit on the arbitrator's powers, but instead on inherent powers. (AOB 39 [contending that the trial court "answered both of these questions" in Downs' favor].) So what? He still lost on the ultimate issue: whether the dismissal with prejudice should be vacated.

What's more, the trial court did not abuse its discretion in determining that the requested $320,000 pertained entirely to that issue.

(16 AA 4429.) Downs asserts that he incurred these "substantial" sums "in responding to Rice and Day's untimely and unauthorized Opposition and Reply filings in October 2014, by which Rice and Day sought to vacate the *entire* Award and which the Superior Court found were untimely and improper." (AOB 39, emphasis in original, citing 7 AA 1834-1835.)

Yet again, not so.

Rice and Day filed a timely petition to partially vacate the award. (See 5 AA 1276 [Downs concession that Rice's petition was timely].) But after their new counsel discovered the evidence proving Downs' misstatements, they raised that issue in a short opposition to Downs' petition to confirm and asserted that the award should be either partially or completely vacated. (5 AA 1267-1268.) Rice and Day's reply in support of their timely petition to vacate addressed that same issue. (5 AA 1285-1294.) The trial court agreed that the opposition brief was untimely and refused to consider vacatur of the entire award. (7 AA 1834-1835.) But the remainder of the trial court's order makes clear that the issue itself—fraud and undue means arising from Downs' discovery conduct and misstatements—was properly before the court. Contrary to what Downs says, the court never suggested that Rice and Day's reply brief or the substantive issues it discussed were "untimely," "unauthorized" or "improper." (AOB 39 [citing only order finding that the opposition was

untimely].) The court even requested supplemental briefing of those substantive issues. (See 7 AA 1831-1846.)[10]

The trial court didn't abuse its discretion in determining that Downs did not incur $320,000 in opposing complete—as opposed to partial—vacatur. Rice's opposition brief was less than two pages. (5 AA 1266-1268.) Downs' responded with just two paragraphs arguing that Rice's opposition was untimely. (5 AA 1275-1276.) The balance of his 8 page "objection" to Rice's opposition argued the merits of the fraud and undue means argument—the same arguments that Downs made in his supplemental briefs filed pursuant to the court's order for further briefing, following which the trial court ordered partial vacatur. (5 AA 1276-1282.) It is hardly surprising that the trial court did not treat that as additional, successful work worthy of a fee award.

At most, Downs was the prevailing party as to his petition to confirm and the losing party as to Rice and Day's petition to partially vacate the award. Downs theorizes that the trial court "necessarily determined" that he was "the prevailing party" because the court awarded him $13,500 in fees and costs. (AOB 39.) But the trial court made that award *before* it decided whether to partially vacate the award—indeed, at the same time that it requested supplemental briefing to decide the petition to partially

[10] The trial court's order states that "there was no timely correction or petition to vacate." (7 AA 1835.) But the court clearly meant only that the request in the late opposition for full—rather than partial—vacatur was not timely. Anything else renders incomprehensible the trial court's consideration of vacatur issues.

vacate. (7 AA 1844-1846 [requesting supplemental briefing while awarding some fees to Downs]; 16 AA 4429-4430 [in order deciding to partially vacate, noting that court had previously "awarded Downs $13,500 in fees and costs" while denying Downs' additional request].)

CONCLUSION

It is time for Rice to have a true opportunity to present his claims on the merits. The trial court erred in ordering those claims to arbitration, given the narrow arbitration provision and the undisputed applicability of section 1281.2(c). And in arbitration, Rice and Day's claims were improperly dismissed with prejudice by virtue of Downs and Nixon Peabody's coordinated campaign to delay and deny Rice and Day's ability to prosecute their claims.

The Court should set aside the order compelling the parties to arbitration so that the claims against Downs and Nixon Peabody can be litigated together. At very least, the Court should affirm the trial court's vacatur decision.

Dated: September 2, 2015

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to California Rules of Court, rule 8.204(c)(1), I certify that the attached **COMBINED RESPONDENT'S BRIEF AND APPELLANT'S OPENING BRIEF** is proportionately spaced and has a typeface of 13 points or more. Excluding the caption page, tables of contents and authorities, signature block and this certificate, it contains 21,215 words.

DATED: September 2, 2015

Jeffrey E. Raskin

PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is 5900 Wilshire Boulevard, 12th Floor, Los Angeles, California 90036.

On September 2, 2015, I served the foregoing document described as: **COMBINED RESPONDENT'S BRIEF AND APPELLANT'S OPENING BRIEF** on the parties in this action by serving:

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Executed on September 2, 2015, at Los Angeles, California.

(State): I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Pauletta L. Herndon