BY SUSAN RABIN AND F. FREDDY SAYEGH

Creating Independent Record Labels for Artists

FOR SOME TIME NOW the music industry has been consolidating, downsizing, and signing fewer artists and songwriters. The industry continues to struggle with piracy, illegal downloading, and the challenge of new technologies. Attorneys who represent musical artists, songwriters, producers, and others with musical ambitions likely have noted the resultant chilling effect and despair among their clients. The doors to the major labels and music publishers were never open wide. Now, fewer doors exist.

One outlet remains, however, for clients who need to find a path to rock stardom: independent record companies. The good news is that there are thousands of independent labels. Some are vanity labels that feature one artist (and may be owned by that artist). Many vanity labels start small but then sign a number of artists and procure national distribution of their recordings (if the music interests the distributor). An indie label with a track record can persuade a major label to handle distribution on a national and even international level. Major labels look to indies to locate new and edgy artists. Large and small companies may work together on joint venture releases. Sometimes, a major acquires the indie as an affiliate.

Advising clients to form an independent record company is relatively easy. Many steps in formation resemble those taken to form any other type of business. Capital is necessary to establish and conduct the business. The type of entity depends on the client's budget, needs, expertise, and the anticipated size and scope of the business. A sole proprietorship can work if the client knows how to find talent as well as handle business matters such as licenses, applications, and contracts. This form requires applying for a city business license and filing a fictitious name certificate.

A partnership, on the other hand, may work best if one party's strengths are in the creative area and others have a better aptitude for running a business. The city business license and fictitious name filing are again necessary, and a partnership agreement is advisable. A corporation, an LLC, or other form can be considered in weighing financial liability and tax issues. Articles of incorporation and other documents must be filed with the state.

Name clearance and protection are needed to avoid later conflicts and disputes. If a client cannot finance a professional search and trademark application, it is advisable to make as thorough an informal search as possible. In addition to checking registered trademarks (federal and state), clients can research music industry publications, source directories, and online databases. The names chosen should not be similar to other labels, music publishers, distributors, music marketing companies, or other music industry companies.

The client may be the label's only artist for a while. If and when another artist is signed, an exclusive artist recording agreement grants the company rights to record the artist's performances and release records, subject to payment of royalties to the artist. The agreement should include the label's right to shop the recordings to a distributor or other label. Most companies, large or small, will not obligate themselves to release an artist's recordings.

Written agreements are essential to keep the artist from jumping ship after clients have invested in the artist's career. Most agreements provide that the artist's performance and producer's work were rendered on a work-for-hire basis. A producer agreement secures the copyright in the producer's work on the recording. Producers can be hired for a flat fee or for royalty payments on a project-by-project basis. The agreement may grant the producer some creative control over the choice of studio and recording and mixing process.

Rap and hip-hop labels sometimes have staff producers whose talents become synonymous with the label's name. Musicians who are hired only for the particular recording project need to enter into a sideman agreement or service release so that the label owns the copyright and other proprietary rights in their performances. Compensation is usually handled with a flat fee. If a client has sufficient funds, it is advisable to pay parties for the project and thus dispense with the need for future accounting. Clients will need assistance with registering copyrights in the sound recordings and obtaining mechanical licenses for the use of copyrighted music on the recordings. Forms and information are available at www.loc.gov/copyright. Music with or without lyrics is registered on Form PA, and recordings are registered on Form SR.

Independent label clients are well advised to acquire a publishing interest in their artists' songs. Publishing income from various uses of music is often the way the label funds its recording expenses. Publishers have duties to register song copyrights; file clearances with a performing rights society such as ASCAP, BMI, or SESAC; collect earnings; and account to songwriters.

Some artists who are less typically commercial may not get much radio play but can sell if promoted to specialty shops such as the Nature Company, Starbucks, Victoria's Secret, and so on. The Internet has become a fertile ground for marketing independent artists and labels. Until clients have the budget for promotion, they can court the favor of college radio program directors who look for unusual, less mainstream releases. Live performances can be set up at shopping centers, colleges, universities, high schools, athletic events, restaurants, and typical nightclub venues. Local newspapers and underground publications are happy to hear about new creative ventures and should be contacted often. Press reviews are useful to help sell product.

Attorneys for small labels should be careful to avoid potential conflicts of interest when clients bring musicians, producers, songwriters, and others to discussions. In such situations, attorneys should clarify who the client is and encourage everyone else to seek independent legal counsel. In so doing, attorneys may avoid a claim of breach of fiduciary duty.

Perhaps the best focus is to encourage clients that they can create their careers in the music industry. Besides legal input, attorneys can provide their creative clients with support for, and confidence in, their ambitions. ■

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BY MATTHEW C. MICKELSON

Enforcement of Binding Arbitration Provisions in Retainers

MOST ATTORNEYS REQUIRE their clients to sign a retainer agreement setting forth the basic scope of the lawyer's representation, the hourly rate to be charged, and other important issues. Retainer agreements are mandatory if the attorney is representing a client on a contingency basis.[1] The typical retainer agreement often includes a binding arbitration provision, requiring any dispute that arises between client and lawyer to be adjudicated conclusively before a neutral arbitrator.

Since the enactment of the California Arbitration Act (CAA),[2] California courts have strongly supported the enforceability of arbitration agreements.[3] Given the courts' powerful endorsement of contractual arbitration, many attorneys might feel reasonably secure in believing that a fee-related dispute with a client would be controlled by a mandatory binding arbitration clause included in a retainer agreement. In fact, however, statutory and case law has created large uncertainties as to whether or not binding retainer agreements are enforceable when clients and lawyers have a dispute over unpaid fees. Attorneys must tread carefully when they embark upon any kind of fee-related litigation with a client and must take care if they wish to have an eventual arbitration award made enforceable.

Attorneys must tread carefully when they embark upon any kind of fee-related litigation with a client and must take care if they wish to have an eventual arbitration award made enforceable.

The complicating factor is the Mandatory Fee Arbitration Act (MFAA).[4] First adopted in 1978, the MFAA constitutes a distinct arbitration scheme that exists solely for the resolution of fee disputes between attorneys and clients.[5] It provides clients the statutory right to invoke mandatory arbitration in fee disputes with their attorneys.[6] However, any award made in such an arbitration will be nonbinding unless both parties agree in writing to be bound *after* the dispute over fees and costs has arisen.[7] The differences between MFAA arbitration and traditional arbitration under the CAA are evident. Arbitration under the MFAA can be commenced by a client without any prior agreement by the parties to resolve their dispute outside the court system, whereas such an accord is required under the CAA.[8] Moreover, arbitration under the MFAA will only be binding if, after the development of a fee dispute between the parties, they choose for it to be so. This situation is very different from most commercial arbitrations.[9]

After a few years of practice under the statute, lawyers began to notice that there was a possible conflict between the CAA and the MFAA. This issue became especially prominent after 1996, when the MFAA was amended to state that arbitration could only be made binding if both parties agreed "after the dispute over fees, costs, or both, has arisen."[10] Specifically, the CAA's provisions allowing the enforceability of precontroversy binding arbitration agreements and the MFAA's requirement that postdispute arbitrations invoked by clients must be nonbinding without both parties' consent seemed to be incompatible. The conflict was not addressed in any appellate court decision until 1998. That year, the Fourth Division of the First District Court of Appeal decided *Alternative Systems, Inc.* v. *Carey*,[11] which appeared to put into doubt the viability of binding arbitration provisions in attorney-client fee disputes.

Alternative Systems involved an attorney-client retainer agreement in which both parties agreed to submit any future dispute to binding arbitration before the American Arbitration Association (AAA).[12] After a fee dispute arose, the attorney invoked the arbitration provision and demanded binding arbitration before the AAA. The client demanded a nonbinding arbitration under the MFAA. Nonetheless, it participated in the binding arbitration hearing, appearing to contest the jurisdiction of the AAA. The MFAA arbitration took place first, and both parties filed a rejection of the nonbinding award,[13] which under the MFAA meant that either could have a trial de novo on the fee issue.[14] Later, the binding arbitration was held. The arbitrator entered an award in favor of the attorney, which was then confirmed by the superior court and made into a judgment.[15]

The Attorney Loses on Appeal

The attorney's victory did not survive long. The appellate court vacated the judgment and ordered a trial de novo.[16] It reasoned that the MFAA provided all clients with a nonwaivable right to request nonbinding arbitration after the fee dispute arose, and that, since the client had invoked its MFAA rights, the binding arbitration clause was "preempted."[17] Indeed, the court made it clear that all such clauses were rendered inoperable once the client had demanded MFAA nonbinding arbitration, so long as the arbitration had taken place and the client or lawyer had rejected any award rendered by the arbitrators. The court rejected as a "farfetched notion" the idea that a binding arbitration clause could survive the MFAA process, given that Business and Professions Code Section 6204 "makes it clear that the trial [de novo after rejection of the award] is commenced by a court action and proceeds in accordance with provisions generally pertaining to civil actions."[18]

Alternative Systems appears to provide clients with a way to eviscerate binding arbitration clauses in their retainer agreements. A

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client who does not want to have a fee dispute submitted to binding arbitration can invoke the MFAA at the beginning of a dispute, refuse to agree to binding arbitration, reject the award (if it is negative) in a timely manner, and oppose any petition to compel arbitration after the lawyer has commenced the trial de novo. Conversely, lawyers who were counting upon their arbitration clauses in fee disputes saw them virtually nullified by *Alternative Systems*.[19]

This was the status of the law until 2001, when the Fifth Division of the First District Court of Appeal published *Aguilar* v. *Lerner*.[20] This case concerned a fee dispute and a retainer agreement with a binding arbitration provision.[21] Just as in *Alternative Systems*, a binding arbitration was held and an award was made in favor of the attorney that was confirmed in superior court.[22] The client also filed a malpractice claim against the attorney, a fact that would later become determinative when the supreme court decided to review the decision of the court of appeal.

Unlike the outcome in *Alternative Systems*, however, in *Aguilar* the court of appeal upheld the judgment.[23] The *Aguilar* court seemed to both sidestep and confront the reasoning of *Alternative Systems*. It found that the client was estopped from employing the same argument that the client in *Alternative Systems* had successfully used, since the *Aguilar* client had never invoked its MFAA right to a nonbinding arbitration.[24] Yet at the same time, the *Aguilar* court declared that the MFAA is not "the exclusive mechanism for resolution of fee disputes. Granting finality to the arbitrator's award is indeed consistent with the Legislature's strong support for private arbitration, as articulated in title 9 of the Code of Civil Procedure."[25] As a result of this, the court concluded, "[T]he challenged clause providing for binding arbitration is not violative of 'an explicit legislative expression of public policy' and will not be invalidated on that ground."[26]

With a conflict between the *Aguilar* and *Alternative Systems* decisions now more or less explicit, the California Supreme Court granted review of *Aguilar*. Attorneys and clients hoping to receive a clear statement about enforceability were disappointed, however, when the court released its decision.

Evading the Question

The court's decision acknowledged that the case "poses the question whether the parties' agreement to arbitrate is enforceable or is superseded by the MFAA."[27] But the court's majority opinion[28] then proceeded to evade that question. Instead of resolving the conflict between the lower courts' decisions in *Aguilar* and *Alternative Systems*, the court decided the matter on a limited basis. Since the client in *Aguilar* had filed a malpractice lawsuit against his attorney, the court concluded that he had waived all of his rights under the MFAA, and that therefore the binding arbitration clause was operative and enforceable.[29] As for the central issue of the case, the court declined to address it: "Because plaintiff waived his MFAA rights, we have no occasion to address whether or to what extent an arbitration agreement is enforceable if a client properly invokes the right to arbitrate under the MFAA, but subsequently exercises his statutory right to reject the arbitrator's decision and have a trial de novo."[30] The majority decision therefore left *Alternative Systems* and the appellate decision in *Aguilar* alive. The confusion over the enforceability of binding arbitration agreements in attorney-client retainer agreements persisted.

Nevertheless, the decision left some palpable hints as to what the supreme court may do if it addresses this issue again in the near future. A reading of those tea leaves puts the continued viability of *Alternative Systems* in doubt. A strong concurring opinion in *Aguilar,* written by Justice Ming W. Chin,[31] argued that the court should have upheld the enforceability of the binding arbitration provision, stating that the invocation of nonbinding arbitration and the request for a trial de novo does not preempt an earlier arbitration clause but simply constitutes a complementary set of procedures that may or may not resolve an attorney-client dispute before it proceeds further.[32] Despite some inconsistencies in the wording of the MFAA, the concurrence argues that, taken as a whole, it must be read to permit the enforcement of a binding arbitration clause, especially given the fact that the *Alternative Systems* rationale gives the client the option of evading such a clause by simply invoking nonbinding arbitration.[33] The concurring opinion concludes that the majority has effectively overruled *Alternative Systems*, and that the court should do so explicitly.[34] In addition, a second concurring opinion written by Justice Carlos R. Moreno agreed that "there is no incompatibility between the [MFAA and CAA], at least in this case," but, like the majority, refused to decide the issue of the viability of predispute binding arbitration provisions.[35]

In the wake of the *Aguilar* decision, attorneys have to continue to be very careful about invoking binding arbitration agreements in any fee dispute with their clients. The case law is clear that if the client commences litigation against the lawyer, launches the binding arbitration process, or participates "voluntarily" in a binding arbitration session, any award resulting from the process will be valid, regardless of the MFAA.[36]

The difficulty arises in cases in which MFAA arbitration is invoked but either party refuses to accept any award as binding. Calling for a trial de novo and then commencing binding arbitration procedures is risky for the lawyer. If the client properly objects, any award granted to the lawyer could later be vacated under *Alternative Systems,* which is still officially good law under *Aguilar.* The choices available to a lawyer confronted with this situation are to continue with the regular judicial process to a verdict or to press on with the arbitration and convince a judge or the appellate court that the arbitration was valid.

Lawyers selecting the second option can garner encouragement from Chin's concurring opinion in *Aguilar*. Its reasoning seems sounder than that of *Alternative Systems* and more likely to fit into the supreme court's preference for harmonizing statutes rather than determining that the legislature has implicitly repealed a previous law.[37] The Chin concurrence, should it be adopted by the court as a whole, would also serve to obviate the gamesmanship that is permitted by the *Alternative Systems* decision, under which a client who previously agreed to binding arbitration may evade his or her commitment by employing procedural tactics. The *Aguilar* majority clearly showed its distaste for similar maneuvers by rejecting the client's argument there that the MFAA could be invoked to short-circuit a CAA arbitration after he had already waived his MFAA rights.[38]

The question ultimately becomes whether an attorney believes a binding arbitration hearing is so much preferable to court that it outweighs the possible need to go to the appellate court (and possibly the supreme court) if an award is vacated at the trial level. Attorneys may someday get some clarity from the supreme court about attorney-client binding arbitration provisions. Until then, attorneys in fee disputes with clients that involve the binding arbitration provisions in their retainers should proceed with full knowledge of the possible consequences of their actions. ■

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[1] *See* BUS. & PROF. CODE §§6147, 6148. Even when a written retainer agreement is not required, a written explanation of the fee agreement is preferred. MODEL RULES OF PROF'L CONDUCT R. 1.5(b).

[2] CODE CIV. PROC. §§1280 *et seq.*

[3] The California Supreme Court has declared that there is a "strong public policy in favor of arbitration as a speedy and relatively inexpensive means of dispute resolution." Moncharsh v. Blase, 3 Cal. 4th 1, 9 (1992). Arbitrators' decisions are generally unreviewable for legal error (*id.* at 11), and even the issue of whether an arbitration agreement was induced by fraud can be adjudicated in the arbitrarion process. Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak St., 35 Cal. 3d 312, 323 (1983).

[4] Mandatory Fee Arbitration Act (codified at BUS. &