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The Court's Power to Grant Preliminary Injunctions in C ases Where Arbitration is Pending

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THE COURT'S POWER TO GRANT PRELIMINARY INJUNCTIONS IN CASES WHERE ARBITRATION IS PENDING

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I. INTRODUCTION

In *Janvey v. Alguire*, the Fifth Circuit was forced to confront the circuit split regarding a court's ability to exercise its equitable powers in granting injunctive relief while an order to compel arbitration is pending.[1] *Janvey* is the latest case in the saga of Courts trying to reconcile the Federal Arbitration Act's policy favoring arbitration with the Court's traditional equitable role.[2] Preliminary injunctive relief is used to prevent injury while a case is pending; however, this remedy is problematic when it involves the interaction of the public court system and a private agreement to arbitrate.[3] Courts considering a motion for preliminary injunction while arbitration is pending face a dilemma accompanied by unclear jurisprudence.

Even without the added question of arbitration, proving the requisite elements necessary to receive a preliminary injunction can be a daunting task. A plaintiff must establish four elements:

> (1) a substantial likelihood of success on the merits, (2) a substantial threat of irreparable injury if the injunction is not issued, (3) that the threatened injury if the injunction is denied outweighs any harm that will result if the injunction

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[1] Janvey v. Alguire, 628 F.3d 164, 172 (5th Cir. 2010).
[2] *Id.* at 173.
[3] *Id.*

> is granted, and (4) that the grant of an injunction will not disserve the public interest.[4]

An individual need not show that he or she will win his or her case but in order to satisfy the first element he or she must demonstrate a *prima facie* case.[5] Traditionally, the second element of irreparable harm applies where monetary damages are not adequate, but may also be used to prevent the dispensation of corporate funds so as to prevent insolvency.[6] The third and fourth elements require the court to balance the interests of both parties and the public.[7] Only after these four elements are addressed may the court then evaluate the appropriateness of injunctive relief in regard to arbitration.[8]

II. THE FIRST CIRCUIT

In *Teradyne, Inc. v. Mostek Corp*., a contract dispute arose between a semiconductor supplier and a laser manufacturer.[9] The district court granted a preliminary injunction, enjoining Mostek from selling the bulk of its assets and rendering itself judgment proof.[10] The injunction Teradyne requested was granted pending the outcome of arbitration.[11] The First Circuit, following the precedents of the Second, Fourth, and Seventh Circuits and declining to follow the Eighth Circuit, held that preliminary injunctive relief is proper in order to preserve the status quo even in the face of arbitration.[12]

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[4] *Id.* at 174.
[5] *Id.*
[6] *Janvey*, 628 F.3d at 179-80.
[7] *Id.* at 180.
[8] *Id.* at 181.
[9] Teradyne, Inc. v. Mostek Corp., 797 F.2d 43, 45 (1st Cir. 1986).
[10] *Id.* at 52.
[11] *Id.* at 45.
[12] *Id.* at 51.

The First Circuit, like all courts faced with the question of whether to grant injunctive relief in the face of pending arbitration, must reconcile its holding with the precedent set by the Supreme Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*[13] In *Moses H.* Cone, the Supreme Court espoused a federal objective of favoring arbitration regardless of state law.[14] The First Circuit found, that unlike in *Moses H. Cone,* the process of arbitration was not affected in *Teradyne* because a party sought to stay arbitration in *Moses H. Cone*, whereas here, a party sought to preserve a remedy pending a ruling on whether arbitration was to be compelled.[15] By preserving the status quo in granting preliminary injunctive relief where the appropriate elements are met, the court believed it was preserving the meaningfulness of arbitration and was thus is in line with the Congressional intent of the Federal Arbitration Act.[16]

III. THE SEVENTH CIRCUIT

In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Salvano,* the Seventh Circuit addressed a courts ability to grant injunctive relief in a case where arbitration was pending.[17] *Salvano* involved a dispute in which employees of Merrill Lynch resigned in favor of employment with a new firm; Merrill Lynch subsequently sought an injunction preventing the now ex-employees from soliciting clients or disclosing client information.[18] Merrill Lynch obtained the injunction sought, which Salvano attempted to have dismissed a number of times

[13] *Id.* at 49 (citing Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 22 (1983)).
[14] THOMAS E. CARBONNEAU, ARBITRATION LAW IN A NUTSHELL 2D ED., 106 (Thomson/West 2009).
[15] *Teradyne*, 797 F.2d at 49-50.
[16] *Id.* at 51.
[17] Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Salvano, 999 F.2d 211, 212 (7th Cir. 1993).
[18] *Id.*

during the course of arbitration.[19] Merrill Lynch proved the requisite elements to obtain an injunction and the Seventh Circuit agreed with the Second Circuit's contention that granting a preliminary injunction preserves the meaningfulness of arbitration.[20] This preliminary injunction, like the others discussed *infra*, was applicable only for the period leading up to the point where arbitration was compelled.[21]

IV. THE EIGHTH CIRCUIT

In another case involving Merrill Lynch, *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Hovey,* the Eighth Circuit addressed nearly identical issue as the Seventh Circuit in *Salvano*.[22] The Court in *Hovey* first addressed the issue of arbitrability before addressing the appropriateness of injunctive relief.[23] As a member of the New York Stock Exchange, Merrill Lynch was required to submit its dispute with Hovey to arbitration as per rule 347 of the New York Stock Exchange.[24] The Eighth Circuit focused first on the question of arbitrability before addressing the preliminary injunction, finding that arbitration agreements should be construed liberally so that doubt regarding the scope of the arbitration agreement should be construed in favor of arbitration.[25] Unlike the Seventh Circuit in *Salvano*, the Eighth Circuit held that where a dispute is arbitrable, the court must look to the terms of the agreement in order to determine the appropriateness of granting a preliminary injunction.[26] The injunction was viewed as an undue delay

[19] *Id.* at 213.
[20] *Id.* at 214.
[21] *Id.* at 216.
[22] Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Hovey 726 F.2d 1286, 1287 (7th Cir. 1993).
[23] *Id.* at 1288.
[24] *Id.* at 1288.
[25] *Id.* at 1289, 1292 (citing Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1 (1983)).
[26] *Id.* at 1292.

or obstruction placed on arbitration by the courts and therefore runs contrary to the purposes of the Federal Arbitration Act.[27] The determinative issue for the Eight Circuit was the actual agreement to arbitrate.[28] Unlike *RGI v. Tucker,* discussed below, the contract in *Hovey* was silent on the issue or preliminary injunctions.[29] These two issues, the Federal Arbitration Acts liberal federal policy favoring arbitration and the lack of agreement by the parties, led the Eighth Circuit to conclude that preliminary injunctive relief under this situation is improper.[30]

It should be noted that the Eighth Circuit may uphold a preliminary injunction in cases where the end result is to possibly shorten the time it takes to compel arbitration.[31]

V. THE FIFTH CIRCUIT

The Fifth Circuit addressed the same issues presented in *Hovey* when it decided *RGI, Inc. v. Tucker & Assocs., Inc.* but distinguished its ruling based on the facts.[32] In *RGI* the Navy contracted with Tucker & Assocs. to manage personnel records and Tucker subcontracted part of its work out to RGI.[33] After an investigation, it was discovered that RGI was in violation of the Federal Fair Labor Standards Act; Tucker & Assocs. withheld payment to RGI pending an audit an RGI brought suit to compel arbitration.[34] Unlike in *Hovey*, the parties in *RGI* laid out specific terms regarding the availability of injunctive relief within their contract.[35] The contract provided in relevant part:

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[27] *Hovey*, 726 F.2d 1286, 1292 (7th Cir. 1993).
[28] *Id.* at 1291.
[29] *Id.* at 1291.
[30] *Id.* at 1292.
[31] In re Y & A Group Securities Litigation, 38 F.3d 380 (8th Cir. 1994).
[32] RGI, Inc. v. Tucker & Assocs., Inc., 858 F.2d 227, 230 (5th Cir. 1988).
[33] *Id.* at 228.
[34] *Id.* at 228.
[35] *Id.* at 230.

> In the event that a dispute is submitted for arbitration pursuant to this paragraph, this Subcontract *shall continue in full force and effect* until such decision is rendered . . . If the Contractor has capability to honor such invoices it shall make such payments as required and the Subcontractor services shall continue until such time as a decision is rendered under this article.[36]

This distinction allowed the Fifth Circuit to address the same issues contemplated by the *Salvano* and *Hovey* courts without taking a position or favoring a jurisdiction.[37] Allowing injunctive relief in *RGI* preserved the status quo as contemplated by the parties, and did not contravene the purposes of the Federal Arbitration Act because the Court simply enforced what was already agreed upon by the parties.[38]

The Fifth Circuit re-addressed the issue of granting a preliminary injunction while arbitration is pending in the recent case of *Janvey v. Alguire*. This case arises out of a Securities and Exchanges Commission investigation that uncovered an alleged multi-million dollar Ponzi scheme.[39] The victims of this alleged Ponzi scheme sought to freeze what assets were remaining in order to preserve the availability of some measure of damages.[40] In *Janvey*, the court faced the issue of whether it could grant preliminary injunctive relief before deciding to compel arbitration.[41] Acknowledging the liberal federal policy favoring arbitration, the Fifth Circuit found that the Federal Arbitration Act provides little guidance regarding preliminary injunctive relief prior to a decision on whether to compel

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[36] *Id.*
[37] *RGI, Inc*., 858 F.2d at 230.
[38] *Id.*
[39] Janvey v. Alguire, 628 F.3d 164, 169 (5th Cir. 2010).
[40] *Id.* at 170.
[41] *Id.*

arbitration.[42] Although preserving the status quo usually has little effect on arbitration, the question most courts face is: How much power does a private agreement to arbitrate take away from the courts and place in the hands of the arbitrator?

The Fifth Circuit agreed with the First Circuit in stating that a preliminary injunction preserving the status quo maintains "the meaningfulness of the arbitration process."[43] This holding, however, is quite limited in that it only applies to the interim time before a court rules on a motion to compel arbitration; after the court compels or denies arbitration, the parties were permitted to ask the courts to reconsider the preliminary injunction. If arbitration were to be compelled, the continuance of the injunction would be a matter for the arbitrator to decide.[44]

VI. CONCLUSION

The circuit split between the Eighth and other circuits was brought to the forefront by the latest Fifth Circuit opinion in *Janvey*.[45] The split still exists because while most circuits will grant a preliminary injunction in the time before arbitration is compelled[46] the Eighth Circuit still holds that granting a preliminary injunction while arbitration is pending is an undue delay to the arbitration process and impermissible under the Federal Arbitration Act.[47] Although the vast majority of circuits follow the reasoning of the Fifth Circuit, one must still be aware of the contrary jurisprudence in the Eighth Circuit.[48] It is important to remember that the courts have not focused on creating a hard and fast rule where injunctive relief is concerned; rather, all the courts have focused on the effect granting injunctive

[42] *Id.*at 173.
[43] *Id.* at 174 (quoting Teradyne v. Mostek Corp., 797 F.2d 43, 51 (1st Cir.1986)).
[44] *Janvey*, 628 F.3d at 172.
[45] *Id.* at 171-72.
[46] *Id.*
[47] Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Hovey 726 F.2d 1286, 1292 (7th Cir. 1993).
[48] *Janvey*, 628 F.3d at 171-72.

relief would have on the pending arbitration. This focus on the effect of granting injunctive relief leaves room for a compelling argument to shift either jurisprudence discussed *infra* by changing the way the effect of injunctive relief is framed.