



Enforcing Your Arbitration Agreement In Federal Court When the Underlying Dispute Cannot Be Removed From State Court

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Introduction

You are defending a claim brought in state court in violation of an arbitration agreement. You would prefer to fight the battle over the enforceability of the arbitration agreement in federal court. But, for any number of reasons, removing the litigation to federal court based on diversity of citizenship is not an option – most typically because the company is a citizen of the state where the action is pending¹ and/or because the plaintiff included an employee who shares citizenship with the plaintiff thereby preventing complete diversity of citizenship.² Since you cannot remove the case to federal court, you will have to seek to enforce the arbitration agreement in the state court where the underlying action is pending, right? Not necessarily.

It may be possible for the state court defendants³ (or some of the state court defendants) to file a separate action in federal court against the state court plaintiffs to compel arbitration pursuant to Section 4 of the Federal Arbitration Act, 9 U.S.C. §§ 1-16 (“FAA”). This article will discuss the most commonly-raised procedural hurdles to such actions in federal court, which are (a) whether the federal court may exercise diversity jurisdiction⁴ to consider the petition to compel arbitration, (b) whether the federal court should decline to invoke its jurisdiction under the *Colorado River* abstention doctrine, and (c) whether the federal court should enjoin the state court plaintiffs from pursuing their claims in state court. These issues are addressed in the recent case of *GGNSC Louisville Hillcreek, LLC v. Warner*, No. 3:13-CV-752-H (W.D. Ky. Dec. 19, 2013).

Does the Federal Court Have Subject Matter Jurisdiction?

It is well-established that the FAA does not itself confer federal question jurisdiction. Therefore, a state court defendant must demonstrate that the federal court has jurisdiction to hear its petition to compel arbitration. For diversity jurisdiction, this means demonstrating that the amount in controversy exceeds \$75,000 and that there is complete diversity between the parties to the federal court action.

Does the amount in controversy exceed \$75,000?

Generally speaking, the amount in controversy is determined by reference to the amount in controversy in the underlying litigation. *Woodmen of the World/Omaha Woodmen Life Ins. Soc’y v. Scarbro*, 129 Fed. Appx. 194, 196 (6th Cir. 2005) (unpublished) (“The true value of arbitration, the object of this [type of] litigation, cannot be determined without reference to the potential cost of the state claim [to the federal court plaintiff].”); see also *CMH Homes, Inc. v. Goodner*, 799 F.3d

¹ 28 U.S.C. § 1441(b)(2) (“A civil action otherwise removable solely on the basis [diversity jurisdiction] may not be removed if any of the parties in interest properly joined and served as defendants is a citizen of the State in which such action is brought.”).

² 28 U.S.C. § 1332(a).

³ Of course, since the state court defendants will be filing the federal court petition to compel arbitration, they would then become the “federal court plaintiffs” and the state court plaintiffs would become the “federal court defendants.” In an attempt to keep things simple and avoid confusion, the parties will be referred to by their state court titles.

⁴ It is well-established that the FAA does not confer federal question jurisdiction. The federal court may exercise federal question jurisdiction with respect to petitions to compel arbitration if the underlying dispute involves federal claims. However, for purposes of this article, we will assume that the underlying dispute does not involve federal claims and that the sole basis for federal jurisdiction is diversity of citizenship.

832, 837-38 (8th Cir. 2013) (extending the holding in *Vaden v. Discover Bank*, 556 U.S. 49 (2009), to hold that, as in cases where subject matter jurisdiction to entertain a FAA petition is premised on the presence of a federal question, to resolve whether diversity jurisdiction exists on a petition to compel arbitration, a court considers whether the amount in controversy between the parties satisfies the jurisdictional minimum by “looking through” to the entire, actual controversy between the parties as they have framed it in state court); *Jumara v. State Farm Ins. Co.*, 55 F.3d 873, 877 (3d Cir. 1995) (“[T]he amount in controversy in a petition to compel arbitration... is determined by the underlying cause of action that would be arbitrated.”). *But see We Care Hair Dev., Inc. v. Engen*, 180 F.3d 838, 841 (7th Cir. 1999) (“Since the present suit is not a removal suit but rather an independent federal suit, it is the stakes of the arbitration and not the possible state court award that control.”). Therefore, the amount in controversy generally can be satisfied by showing that the state court plaintiffs seek damages against the state court defendants in excess of \$75,000.

Is there complete diversity of citizenship?

As noted above, the state court action may not be removable, even though complete diversity exists between the state court plaintiffs and defendants, because one of the state court defendants is a citizen of the state where the state court action is pending. 28 U.S.C. § 1441(b)(2) (“A civil action otherwise removable solely on the basis [diversity jurisdiction] may not be removed if any of the parties in interest properly joined and served as defendants is a citizen of the State in which such action is brought.”). If this is the sole barrier to removal, the issue is fairly simple. All of the state court defendants who are entitled to enforce the arbitration agreement can file a petition to compel arbitration in federal court against all of the state court plaintiffs who are bound by the arbitration agreement, and Section 1441(b)(2) does not come into play because the petition to compel arbitration is a separate action, not a removal.

But what about the situation where removal is impossible because the state court plaintiffs included an employee who is entitled to enforce the arbitration agreement and who shares citizenship with the plaintiff? In this situation, the question is whether the state court defendants who do not share citizenship with any of the state court plaintiffs can petition the federal court to compel arbitration against the state court plaintiffs without including the employee who would break diversity. In any such action, the state court plaintiffs may argue that the missing state court defendant is a necessary and indispensable party under Rule 19 of the Federal Rules of Civil Procedure. In *Warner*, the court concluded that the state court defendant who was absent from the federal action was “necessary,” but not “indispensable” and that the federal court action could, therefore, proceed without including the missing employee. *GGNSC Louisville Hillcreek, LLC v. Warner*, No. 3:13-CV-752-H (W.D. Ky. Dec. 19, 2013). On that issue, the court noted among other things that “‘the possibility of having to proceed simultaneously in both state and federal court,’ or in two separate arbitrations for that matter, ‘is a direct result of [Warner’s] decision to file a suit naming [Golden Gate and Kravis] in state court rather than to demand arbitration under the [ADR Agreement].’” *Id.* (quoting *PaineWebber, Inc. v. Cohen*, 276 F.3d 197, 202 (2001)). Therefore, state court defendants who wish to file a federal petition to compel arbitration against the state court plaintiffs generally will not be required to include any state court defendants who would “break” diversity.

Should the Federal Court Decline to Exercise Its Jurisdiction In Deference to the State Court?

The state court plaintiffs may also argue that the federal court should decline to exercise its jurisdiction in deference to the state court pursuant to *Colorado River Water Conservation District v. United States*, 424 U.S. 800 (1976). But, “abstention from the exercise of federal jurisdiction is the exception, not the rule.” *Warner*, No. 3:13-CV-752-H. The *Warner* court concluded that the state and federal court actions were “parallel,” but that consideration of the applicable factors did not warrant abstention. The court noted that the threat of piecemeal litigation of the arbitration issue in both state and federal courts was created by the state court plaintiff’s choice to name the non-diverse employee in the state court action. *Id.* The court further noted that, while state law would govern the standard contract defenses to the arbitration agreement, “[t]he FAA presents a ‘liberal federal policy favoring arbitration agreements’ that must be taken into account even when state-law issues are presented.” *Id.* (quoting *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983)). The court concluded that “[n]either the fact that the state court could adequately protect Golden Gate’s interests nor the fact that the state possesses concurrent jurisdiction under the FAA is an ‘exceptional’ circumstance necessary to compel this Court to abstain from exercising jurisdiction over this case. *Id.* (citing *Colorado River*, 424 U.S. at 817-818).

Should the Federal Court Enjoin the State Court Plaintiff from Pursuing Claims in a State Court Forum?

The *Warner* court summarized that whether to enjoin a state court plaintiff from pursuing his claims in the state forum “is always a delicate matter, but one which seems clear in this instance.” *Id.* The court noted that “a district court’s injunction of state-court proceedings after compelling arbitration did not violate the Anti-Injunction Act.” *Id.* (citing *Great Earth Co., Inc. v. Simons*, 288 F.3d 878, 893 (6th Cir. 2002)). “[E]njoining the state court proceeding does not offend the Anti-Injunction Act as a matter of law, because it effectuates the proper purposes of this Court’s judgment.” *Id.*

Conclusion

Barriers to removing a claim to federal court will not necessarily prevent state court defendants from enforcing their arbitration agreements in a federal forum. State court defendants can generally file a separate federal action to compel arbitration of the claims pending in state court. However, each case is unique, and careful consideration should be given before filing a separate federal action, particularly where some state court defendants will not be able to participate in the federal action.

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