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Injunction Application May Imply Arbitration Waiver

Including multiple claims in injunction application may preclude later arbitration on those claims

By STUART M. KATZ

Your telephone rings at 4:45 on a Friday afternoon. You answer it, to hear that your client needs an injunction to stop a former employee from violating assorted provisions of her employment agreement, including a covenant not to compete.

Having reviewed the agreement, you know that it contains a provision requiring arbitration of "any and all disputes arising out of, under, or in connection with" the employment agreement. You also know, though, that the covenant not to compete nonetheless grants your client the right to obtain injunctive relief against the former employee in court, in the event of a breach of that provision of the employment agreement.

With this knowledge, you advise the client that you will immediately prepare an application for a temporary injunction to stop the employee from violating the covenant not to compete. The client then tells you that the former employee is also violating the confidentiality, non-disclosure and non-solicitation provisions of the agreement, and that you might as well include those claims, as well as counts for violation of the Connecticut Uniform Trade Secrets Act (CUTSA) and the Connecticut Unfair Trade Practices Act (CUTPA). Armed with this information, you file a multi-count verified complaint in support of the application for temporary injunction.

After a full evidentiary hearing on the non-competition and confidentiality agreement violation claims, the court enters an order for temporary injunction in your client's favor. You then file a motion for stay, pursuant to Conn. Gen. Stat. §52-409, so that the remaining claims against the former employee may be submitted to arbitration.

Not So Fast...

To your (and your client's) great surprise, counsel for the former employee files an objection with the court, asserting that the right to arbitrate has been waived. According to a recent Superior Court decision, that objection may very well be sustained.

In a recent Memorandum of Decision, Superior Court Judge Jon Blue held that because the plaintiff had included certain claims beyond a violation of a covenant not to compete in its complaint filed in support of an application for temporary injunction, the plaintiff had waived its right to compel arbitration of these additional claims.

In the matter of *Multicare Physicians & Rehabilitation Group, PC v. Wong*, 41 Conn. L. Rptr. No. 23, 835 (Oct.16, 2006)), the parties' employment agreement included a broad arbitration provision, reserving the right to seek injunctive relief in court to enforce a non-competition clause in the agreement. The plaintiff filed a multi-count complaint in support of its application for a temporary injunction.

In addition to claiming a violation of the non-competition clause, the plaintiff also alleged violation of a provision governing possession and use of proprietary information, seeking injunctive relief for this count as well. The plaintiff also included counts in its complaint for violating additional provisions of the agreement, plus statutory violations; *i.e.*, CUTPA, CUTSA and computer-related offenses.

The parties agreed to have the court consider the application for temporary injunction as one for a permanent injunction, and the court heard evidence over three days, followed by submission of briefs and oral argument. Following the court's ruling on the application for injunctive relief, the plaintiff filed a motion for stay and referral to arbitration, in accordance with the arbitration provision of the parties' agreement.

Implied Waiver?

The court noted that both parties had agreed that the arbitration provision had been waived as to the plaintiff's request for injunctive relief. However, the court then analyzed whether or not the plaintiff had *impliedly* waived its right to arbitrate the other claims in the complaint.

Without precedent to rely on, Judge Blue considered applicable federal law to determine whether or not waiver of the right to arbitrate had occurred where "part, but not all, of a case has been heard by the court." The Court of Appeals for the 8th Circuit, noted the court, has articulated a three-part test:

The party seeking arbitration may be found to have waived his right to it if he: (1) knew of an existing right to arbitration; (2) acted inconsistently with that right; and (3) prejudiced the other party by those inconsistent acts. *Kelly v. Golden*, 352 F.3d 344, 349 (8th Cir. 2003)(internal quotation marks and citations omitted).

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In the instant case, Judge Blue found that the plaintiff obviously knew of the right to arbitrate, since it was contained in an agreement drafted by the plaintiff. He further found that the plaintiff had "substantially invoked the litigation machinery" in this case, not by seeking injunctive relief with respect to the non-competition clause violations, but by asserting the various other claims in the complaint, which the court deemed "overreaching (for purposes of waiver analysis)."

Simple Matter

Judge Blue notes that it would have been "a simple matter" for the plaintiff to limit its complaint in support of the claim for injunctive relief to the violation of the non-competition provision, and to have left all other matters for arbitration.

Since the plaintiff did not choose that course, and instead "substantially invoke[d] the litigation machinery," the defendant's rights were prejudiced, because the parties spent three days litigating substantial issues on the merits, including the non-competition agreement and the possession of proprietary information claims.

"Compelling arbitration would require considerable duplication of these very substantial efforts," the court concluded, denying the motion for stay and for referral to arbitration.

Cautionary Warning

This decision, without other precedent in Connecticut, should serve as a loud cautionary warning to parties and counsel who seek to obtain injunctive relief for violation of various provisions of written agreements.

First, all should be aware that the right to arbitrate can be waived by implication by a party's conduct. In agreements requiring arbitration, but carving out the right to seek injunctive relief in court for violation of specific provisions, the inclusion of any claims in a lawsuit beyond those specifically carved out in the agreement could jeopardize the right to arbitrate. This is true for claims for which injunctive relief might very well be necessary and appropriate.

Second, given this holding, drafters of employment agreements should pay particular attention to the language included in arbitration provisions, to ensure that parties will have the right to seek injunctive relief for appropriate contractual violations, without waiving the important right to compel arbitration. ■