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SOUTHERN DISTRICT CIVIL PRACTICE ROUNDUP

Expert Analysis

N.Y. Attorney-General Probes, Proper Role of Federal Courts

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The aggressive law enforcement efforts of Attorney General Andrew Cuomo, bolstered by the powerful investigative tools at his disposal, have on occasion been met by equally aggressive resistance from the targets of those investigations.

In at least two recent cases, companies under investigation by the attorney general have sought to challenge the constitutionality of those investigations in federal court—raising the question as to the proper role, if any, that federal courts should play in entertaining constitutional challenges to state investigations.

In both cases, the court refused refuge to the targets of the investigation, but not before the parties engaged in interesting and important procedural wrangling that we discuss more fully below.

'Dreamland Amusements'

Dreamland Amusements Inc., a mobile carnival operating in several states including New York, took two separate routes to federal district court in its effort to derail the attorney general's investigation into its employment practices related to seasonal alien employees working under temporary visas. After initially producing some documents and indicating that it would comply with subpoenas issued by the attorney general, Dreamland filed suit in the U.S. District Court for the Southern District of New York on July 14, 2008 seeking to enjoin the attorney general from proceeding with its investigation.

On July 29, the attorney general filed its own action in New York State Supreme Court, petitioning, by order to show cause, to compel Dreamland to comply with the subpoenas. During the next two weeks, Dreamland moved in federal court for a preliminary and/or permanent injunction and removed the New York state action to federal court, and the attorney general filed a motion to dismiss the federal action and moved by order to show cause to remand to state court the petition to compel compliance with its subpoenas. Southern District Judge John G. Koeltl issued a decision on all three motions in *Cuomo v. Dreamland Amusements Inc.*[1]

> What is the proper role, if any, that federal courts should play in entertaining constitutional challenges to state investigations?

Dreamland hoped that the key to federal court would lie with a form known as an ETA 750A. As required by federal law, Dreamland submitted these forms to the New York State Department of Labor, which in turn forwarded them to the U.S. Department of Labor. The forms contained a pledge by Dreamland to pay its seasonal employees at or above the prevailing wage rate, to refrain from discrimination against the seasonal employees, and that the terms, conditions and occupational environment of the job would be consistent with federal, state and local law. The attorney general had relied in part on information contained in those forms in issuing its investigative subpoenas. Dreamland argued that federal immigration law preempted any state investigation based in whole or in part on construction or interpretation of the ETA 750A forms.

Removal, Preemption

Judge Koeltl first considered whether Dreamland's preemption argument provided a basis for federal subject matter jurisdiction over the removed state court subpoena enforcement action. The attorney general disputed Dreamland's assertion that federal immigration law preempted its investigation, but argued that in any event, preemption would not justify removal under the "well-pleaded complaint rule," which provides that a case arises under federal law for the purposes of federal question subject matter jurisdiction only if the federal claim appears on the face of the well-pleaded complaint. Quoting *Franchise Tax Board v. Construction Laborers Vacation Trust*,[2] Judge Koeltl observed that ordinarily "'a case may not be removed to federal court on the basis of a federal defense, including the defense of preemption….'" He recognized, however, that the "artful pleading doctrine" provides a limited exception to the "well-pleaded

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complaint rule" where a plaintiff attempts to avoid federal jurisdiction by artfully pleading what is in essence a federal claim as though it arises under state law.

In such cases, federal question jurisdiction may exist where a claim pleaded under state law is not merely preempted, but "completely preempted" by federal law. As described by the U.S. Court of Appeals for the Second Circuit in *Sullivan v. American Airlines Inc.*,[3] "[u]nder the complete-preemption doctrine, certain federal statutes are construed to have such 'extraordinary' preemptive force that state-law claims coming within the scope of the federal statute are transformed, for jurisdictional purposes, into federal claims, i.e., completely preempted."

In determining whether the attorney general's petition to compel compliance with its subpoenas was "completely preempted," Judge Koeltl noted that the Supreme Court has only recognized three statutes that completely preempt state law claims (the Labor-Management Relations Act, the Employee Retirement Income Security Act, and the National Bank Act), and that the Second Circuit has added only one additional statute to that list (the Copyright Act). Judge Koeltl observed that the action removed in this case was brought under N.Y. CPLR §2308(b), which authorizes the issuer of a subpoena to move in New York Supreme Court to compel compliance; that the subpoenas themselves were issued under the N.Y. Executive Law §63(12) authorizing the attorney general to investigate and seek to enjoin business from engaging in fraud; and that the attorney general had identified a number of state laws (including state record-keeping, wages, hours and anti-discrimination laws) that Dreamland may have violated.

Stressing the distinction between preemption (a defense that could be asserted in state court) and complete preemption (required to remove the state court proceeding to federal court), Judge Koeltl rejected Dreamland's contention that federal immigration law provided a basis for the assertion of federal subject matter jurisdiction over the attorney general action to compel compliance with the investigative subpoenas. He observed that the federal immigration laws were not on the short list of statutes already recognized as completely preemptive, and that a statute could only be added to that list where federal law provides remedies that completely displace state remedies. He found that Dreamland had shown "nothing of the sort here," observing that "it would be remarkable if Congress had silently displaced all state laws with respect to the protection of workers if the workers were aliens." Id. at *5.[4] Judge Koeltl remanded the attorney general's action to state court.

Ripeness and 'Younger'

Turning to the attorney general's motion to dismiss Dreamland's federal suit to enjoin the investigation,[5] Judge Koeltl granted that motion on two independent grounds. First, he found that the question of whether the investigation was preempted by federal law was not ripe for judicial review. He explained that the ripeness inquiry involved evaluation of the "fitness" of the issues for judicial decision and the hardship to the parties from withholding court consideration. Noting that the fitness inquiry turns on "'whether the issues sought to be adjudicated are contingent on future events or may never occur,'"[6] he concluded that it was "entirely possible that if a prosecution ever occurs, it will not make use of the ETA 750A forms" noting that "many of the alleged wrongs under investigation, including employment discrimination, would violate state law regardless of whether they also violated the terms of the…forms."

The three conditions for 'Younger' abstention: (1) an ongoing state proceeding; (2) implicating an important state interest; and (3) affording an adequate opportunity for judicial review of the federal constitutional claims.

Judge Koeltl also held that the *Younger v. Harris*[7] abstention doctrine provided alternative grounds for dismissal. He outlined the three conditions for *Younger* abstention: (1) an ongoing state proceeding; (2) implicating an important state interest; and (3) affording an adequate opportunity for judicial review of the federal constitutional claims.[8]

Judge Koeltl adopted the approach previous taken by Chief Southern District Judge Kimba M. Wood in *J. & W. Seligman & Co. v. Spitzer*,[9] finding that the issuance of subpoenas by the attorney general seeking information that may be used to commence civil or criminal proceedings against the federal plaintiff qualifies as an ongoing state proceedings for the purposes of *Younger* abstention. He held that "[b]ecause *Younger* abstention is rooted in principles of federalism and comity…and the state's interest in this case in investigating and possibly prosecuting those who commit crimes within its borders implicates those principles, the subpoenas sufficed to initiate an ongoing state proceeding." He found, in the alternative, that the attorney general's motion to compel satisfied the ongoing state proceeding requirement, notwithstanding Dreamland's argument that because that motion was filed after Dreamland commenced its federal action, the motion did not qualify as an ongoing proceeding.

Judge Koeltl concluded that the Supreme Court's decision in *Hicks v. Miranda*[10] squarely controlled this question when it ruled that "where state…proceedings are begun against the federal plaintiffs after the federal complaint is filed but before any proceedings of substance on the merits have taken place in the federal court, the principles of *Younger v. Harris* should apply in full force."

Judge Koeltl went on to find that the attorney general clearly satisfied the "important interest" component of the doctrine, observing that "[a] state's interest in enforcing its own laws and investigating their violation cannot seriously be disputed." Finally, he held that the third prong of the *Younger* inquiry was satisfied because Dreamland could have raised its preemption arguments in state court through a motion to quash the subpoenas or as a defense to the pending motion to compel.

'Arbitron'

Southern District Judge Denise L. Cote's decision in *Arbitron Inc. v. Cuomo*,[11] also relied on *Younger* abstention in dismissing a similar attempt to enjoin an investigation by the attorney general. In that action, radio audience ratings publisher Arbitron Inc. sought a federal temporary restraining order (TRO) and injunction against an investigation by the attorney general, which had announced its intention to sue Arbitron over concerns that a new Arbitron rating program under-represented minority households and threatened a revenue decline for radio stations directed at minorities. Again, the parties engaged in procedural jockeying before the federal action was dismissed in favor of state court proceedings commenced by the attorney general.

Arbitron began a gradual shift from a paper diary rating system to an electronic

meter system in 2007, announcing that the electronic system would become "currency" used to set New York advertising prices on Oct. 8, 2008. On Sept. 9, 2008, the attorney general advised Arbitron that it was investigating Arbitron's deployment of this new technology under New York's false advertising, deceptive trade practices and commercial fraud statutes.

On Oct. 2, 2008, after Arbitron produced documents in response to subpoenas, the attorney general notified the company that the attorney general intended to bring suit, giving the company five days to show cause why such a proceeding should not be instituted. In response, Arbitron advanced the start date for publication of its New York ratings under the new system from the planned date of Oct. 8 to Oct. 6, 2008, and commenced an action in federal court under 42 U.S.C. §1983 asserting that the attorney general's efforts to restrain publication of its audience ratings violated the First Amendment. At an immediate hearing on Arbitron's application for a TRO, the attorney general agreed not to seek any ex parte relief against Arbitron in state court, and to provide Arbitron an opportunity to be heard before any relief requested by the attorney general was granted. Based upon those representations, the request for a TRO was denied.

The attorney general then commenced its anticipated lawsuit against Arbitron in New York Supreme Court, asserting claims under New York's Executive Law, Civil Rights Law and General Business Law and seeking restitution, penalties, fees and a permanent injunction. The attorney general also moved to dismiss Arbitron's federal action.

Judge Cote granted the motion to dismiss on the grounds of *Younger* abstention, noting that while district courts generally "have a 'virtually unflagging obligation to exercise the jurisdiction given them,' … *Younger* and its progeny delineate an exception to this rule, requiring federal courts to abstain where appropriate to 'allow state courts to resolve pending matters within their jurisdiction.'"[12] Plaintiffs disputed the application of *Younger,* arguing that the "ongoing state proceeding" requirement was not satisfied because the federal action was commenced four days before the attorney general filed the state court proceeding. Citing *Hicks,* Judge Cote held that *Younger* abstention was nevertheless appropriate because no proceedings of substance had occurred by the time the state court action was filed. As in *Hicks,* the only proceedings in the federal action had been a denial of the TRO, which she contrasted to the granting of preliminary injunctive relief—a proceeding of substance on the merits that would bar abstention under *Younger*. Thus, by agreeing to refrain from ex parte action rather than risking entry of a TRO, the attorney general may well have preserved its ability to obtain dismissal of that action under *Younger*.

Arbitron also argued unsuccessfully that the attorney general's investigation did not implicate an important state interest. Relying on the Second Circuit's decision in *Philip Morris Inc. v. Blumenthal*[13] for the proposition that abstention is not appropriate where the state seeks monetary relief that would be available to a private citizen, Arbitron asserted that the attorney general had merely substituted itself for the minority radio stations, and that this essentially private dispute did not implicate "central sovereign functions" of the state so as to warrant abstention.

Judge Cote rejected this argument, finding that the attorney general's lawsuit advanced important state interests including the enforcement of state laws against discrimination and deceptive practices, and that the suit may protect the health of radio stations serving the minority community and prevent dissemination of unreliable data. She concluded that the fact that private parties could sue under the same statutes did not eliminate the important state interests implicated by the attorney general's suit—and that in any case, the lead claim in the complaint was brought under Executive Law §63(12), which gives the attorney general sole authority to sue to restrain repeated fraudulent commercial activities.

Conclusion

Although neither Dreamland nor Arbitron has yet completely abandoned hope in light of the fact that both have recently filed Notices of Appeal, these decisions provide little comfort to targets of attorney general investigations hoping for federal court intervention. It remains to be seen whether the Second Circuit will construe *Younger* as presenting almost insurmountable obstacles to those seeking federal review of the attorney general's investigative efforts.

1. 2008 WL 4369270 (S.D.N.Y. Sept. 22, 2008). Dreamland filed a Notice of Appeal on Oct. 20, 2008.

2. 463 U.S. 1, 14 (1983).

3. 424 F.3d 267, 272 (2d Cir. 2005).

4. Judge Koeltl similarly rejected Dreamland's argument that the Fair Labor Standards Act provided a basis for removal, noting that the act did not meet the requirements for complete preemption and that the state court could adjudicate whether Dreamland qualified for an exemption from that statute for its seasonal employees.

5. Judge Koeltl noted that Dreamland had styled its requested relief as an injunction to prevent the attorney general from proceeding with an "ongoing civil and potentially criminal prosecution." Because there was no prosecution of Dreamland, he construed the request as one aimed at the investigation and the possibility of a future prosecution based on that investigation. 2008 WL 4369270 at *2 n.3.

6. Id. at *8 (quoting *New York Civil Liberties Union v. Grandeau*, 528 F.3d 122, 132 (2d Cir. 2008)).

7. 401 U.S. 37 (1971).

8. Id. at *9 (quoting *Diamond "D" Const. Corp. v. McGowan,* 282 F.3d 191, 198 (2d Cir. 2002)).

9. 2007 WL 2822208 (S.D.N.Y. Sept. 27, 2007).

10. 422 U.S. 332, 349 (1975).

11. 2008 WL 4735227 (S.D.N.Y. Oct. 27, 2008). Arbitron filed a Notice of Appeal on Oct. 31, 2008.

12. Id. at *3 (quoting *Royal and Sun Alliance Ins. Co. of Canada v. Century International Arms Inc.,* 466 F.3d 88, 92 (2d Cir. 2006) and *Washington v. County of Rockland,* 373 F.3d 310, 318 (2d Cir. 2004)).

13. 123 F.3d 103 (2d Cir. 1997).