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Judge Blocks Auction-Rate Arbitration against Goldman.

NEW YORK (Reuters) – Goldman Sachs Group Inc has won a court order blocking a North Carolina utility from moving forward with an arbitration before the Financial Industry Regulatory Authority over the extent the bank misled it about auction-rate securities.

U.S. District Judge Paul Engelmayer in Manhattan entered a preliminary injunction Monday preventing North Carolina Municipal Power Agency Number One from proceeding with the arbitration.

In making his ruling, Engelmayer pointed to decisions earlier in 2013 by two different judges in New York presiding over similar cases over auction-rate securities, in which the arbitrations were blocked because of forum selection clauses in broker-dealer agreements.

“The court agrees with their analysis and reasoning; and applies them here,” Engelmayer wrote.

Lawyers for Goldman and the North Carolina utility did not respond to requests for comment.

The case was one of a number filed in the wake of the global financial crisis of 2007 and 2008 by large institutions and investors seeking to bring cases before FINRA.

While arbitration has historically been seen by critics as defense-friendly, some plaintiffs viewed FINRA as attractive because of the speed it hears cases and the difficulty defendants face in overturning an arbitration award on appeal.

Of the 10 largest U.S. securities arbitration awards, seven were issued since 2008, according to Securities Arbitration Commentator Inc.

The case against Goldman stemmed from the North Carolina utility’s issuance of $149.7 million in auction-rate securities underwritten by the bank.

Auction-rate securities were a type of bond in which interest rates were set through bidding by investors. The market for the securities froze in February 2008 when banks ceased propping it up with support bids.

The agency, which provides wholesale power to 19 cities in North Carolina, filed the arbitration in December 2012 accusing Goldman of misrepresenting its role in supporting the market.

The bank, through lawyers at Sullivan & Cromwell, subsequently filed a federal lawsuit seeking to block the arbitration.

Among other arguments, the bank contended that the North Carolina utility waived its right to arbitrate by signing a broker-dealer agreement containing a forum selection clause requiring disputes to be litigated in federal court in New York.

‘PRECLUDE ARBITRATION’

In a 17-page decision, Engelmayer said the agreement “provides ‘positive assurance’ that the parties intended to preclude arbitration.”

Engelmayer also found the auction-rate securities issuance “constitutes a ‘transaction contemplated’ by the broker-dealer agreement and, as such, falls within the scope of the forum selection clause.”

He said the claims were also tied to the broker-dealer agreement. Goldman acted not just as underwriter but also broker-dealer, he said.

“NCMPAI cannot wish away the terms of the broker-dealer agreement when its claims are based on Goldman’s actions as a broker-dealer,” Engelmayer said.

The ruling follows a similar case in which Goldman blocked an auction-rate securities arbitration brought by Golden Empire Schools Financing Authority and Kern High School District in California.

Engelmayer relied in large part on that case, decided by U.S. District Judge Richard Sullivan in February, as well as a decision in May blocking an arbitration by a related North Carolina utility against Citigroup Inc.

The claimants in both Goldman cases and the Citigroup dispute are all represented by James Swanson, a lawyer at Fishman Haygood Phelps Walmsley Willis & Swanson.

The firm has brought several other big cases before FINRA against banks related to auction-rate securities. And while judges in New York have tended toward blocking the arbitrations, other courts have been receptive to the arguments of Fishman Haygoods’ clients.

In January, the 4th U.S. Circuit Court of Appeals allowed Carilion Clinic of Roanoke, Virginia, to proceed with an arbitration against UBS AG and Citigroup over $234 million in auction-rate securities.

A month later, a judge in Minneapolis refused UBS AG’s request to enjoin an arbitration by Allina Health System arising out of $125 million in auction-rate securities it issued in 2007.

The case is Goldman Sachs & Co v. North Carolina Municipal Power Agency Number One, U.S. District Court for the Southern District of New York, No. 13-01319.

For Goldman Sachs: David Braff and Matthew Schwartz of Sullivan & Cromwell.

For North Carolina Municipal Power Agency Number One: James Swanson of Fishman Haygood Phelps Walmsley Willis & Swanson; and Peter Mougey and James Kauffman of Levin Papantonio Thomas Mitchell Rafferty & Proctor.

By Nate Raymond

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