Published on *The National Law Review* https://natlawreview.com

Ninth Circuit's Reversal Allows Mandatory Employment Arbitration Agreements in California

Article By:

Paul R. Lynd

Natalie C. Kreeger

In another reversal of course, the US Ninth Circuit Court of Appeals cleared the way again for California employers to require arbitration agreements. The latest 2-1 decision in Chamber of Commerce v. Bonta, issued on February 15, upheld a district court's preliminary injunction blocking Assembly Bill 51.

That law sought to prohibit employers from requiring employees or job applicants to sign arbitration agreements as a condition of employment. An earlier decision by the Ninth Circuit panel reversed the preliminary injunction. For now, California employers thus may require arbitration agreements. Yet, they still may want to be cautious until the litigation plays out further.

Brief Background on AB 51

The California Legislature approved AB 51 to protect employees from "forced arbitration." As we previously wrote, Governor Newsom signed AB 51 into law in October 2019. The bill added new Labor Code Section 432.6, prohibiting employers from requiring employees or job applicants to waive, as a condition of employment, "any right, forum, or procedure" for a violation of the California Fair Employment and Housing Act or Labor Code. AB 51 also prohibits employers from retaliating against current employees or job applicants for refusing to waive such rights. *See* Labor Code Section 432.6(b). In addition, AB 51 created criminal penalties against employers for violating the law, including up to six months imprisonment and a $1,000 fine. AB 51 applies to any arbitration agreement entered into, modified, or extended on or after January 1, 2020.

As the Ninth Circuit noted, in an odd twist, AB 51 criminalizes only the formation of an arbitration agreement. Thus, an employer could be subject to criminal liability for requiring someone to enter into an arbitration agreement, but the resulting agreement still would be enforceable.

Litigation Against AB 51

Shortly before AB 51's effective date, the US Chamber of Commerce and other business groups sued in federal district court in the Eastern District of California. They sought a declaration that the

Federal Arbitration Act (FAA) preempts AB 51. The federal court in Sacramento granted a temporary restraining order, followed by a preliminary injunction. It held that the plaintiffs were likely to succeed on their preemption argument, because AB 51 "treats arbitration agreements differently from other contracts" and "conflicts with the purposes and objectives of the FAA." The state appealed.

On appeal, in a 2-1 decision in September 2021, the Ninth Circuit reversed and vacated the preliminary injunction. However, it affirmed the district court's preliminary injunction insofar as AB 51's civil and criminal penalties. The plaintiffs filed a petition for rehearing *en banc*. In February 2022, the Ninth Circuit announced it would postpone ruling on the petition until after the US Supreme Court's then-pending decision in *Viking River Cruises, Inc. v. Moriana*, which concerned arbitration agreements and claims under California's Labor Code Private Attorneys General Act (PAGA). As we previously wrote, in August 2022, the same three-judge Ninth Circuit panel withdrew its 2021 opinion and granted a rehearing by the same panel instead.

The Ninth Circuit's New Decision: The FAA Preempts AB 51

After reconsideration, the Ninth Circuit issued a new 2-1 opinion. This time, the majority held that the FAA preempts AB 51, and affirmed the district court's preliminary injunction blocking AB 51. The judge who previously dissented wrote the majority opinion now. The new majority reasoned that "[b]ecause the FAA's purpose is to further Congress's policy of encouraging arbitration, and AB 51 stands as an obstacle to that purpose, AB 51 was therefore preempted."

A line of US Supreme Court decisions has held that the FAA preempts state laws that seek to prohibit enforcement of agreements to arbitration certain types of claims. As a way around those precedents, AB 51 sought to attack the formation of arbitration agreements. The Ninth Circuit, though, recognized that the FAA's preemption is "not limited to state rules affecting the enforceability of arbitration agreements, but also extends to state rules that discriminate against the formation of arbitration agreements." It agreed with other federal circuits that the FAA preempts state laws that discriminate against arbitration by discouraging or prohibiting the formation of an arbitration agreement.

While acknowledging that AB 51 does not expressly bar arbitration agreements, the Ninth Circuit held that AB 51 imposes a "severe" burden on the formation of arbitration agreements by imposing civil and criminal sanctions on an employer for entering into such agreements with certain non-negotiable terms. This "deterrence of an employer's willingness to enter into an arbitration agreement is antithetical to the FAA's 'liberal federal policy favoring arbitration agreements,'" according to the court. As a result, the Ninth Circuit concluded that AB 51's "penalty-based scheme to inhibit arbitration agreements before they are formed violates the 'equal treatment principle inherent in the FAA,'" with the law thus preempted in its entirety.

Further, even though the legislation contained a severability clause, the Ninth Circuit rejected the California's argument that the court could sever the criminal provisions of AB 51 and possibly allow the rest of the legislation to stand. Because "all of the provisions of AB 51 work together to burden the formation of arbitration agreements," the court determined that it could not sever any provisions.

Employer Takeaways

This decision represents the latest turn in the stories of AB 51 and California's repeated legislative and judicial attempts to prohibit or limit employment arbitration agreements. Over the years, those efforts have met with multiple reversals by the Supreme Court under the FAA. The Ninth Circuit's new decision again emphasizes the FAA's strong federal policy favoring arbitration, including with

respect to employment claims. It is a positive decision for employers.

Still, employers should keep in mind that the litigation concerning AB 51 is not done yet. The state could request a rehearing *en banc* before an 11-judge Ninth Circuit panel, or appeal to the Supreme Court. The district court also has not yet issued a permanent injunction against AB 51. Thus, in the meantime, California employers may want to exercise caution in requiring mandatory employment arbitration agreements.

National Law Review, Volume XIII, Number 55