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FEDERAL APPEALS COURT BLOCKS CALIFORNIA'S BAN ON MANDATORY ARBITRATION AGREEMENTS: 7 KEY TAKEAWAYS FOR EMPLOYERS

Insights
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A federal appeals court just paved the way for California employers to continue utilizing mandatory arbitration agreements with employees and job applicants. You may be familiar with the litigation roller coaster of California's Assembly Bill 51 (AB 51), which was slated to take effect January 1, 2020, placing a ban on mandatory arbitration in employment in California. Fortunately, right before its effective date, it was temporarily blocked while several business groups proceeded with legal challenges. The 9th U.S. Circuit Court of Appeals initially upheld parts of the law – but yesterday it fully blocked AB 51, concluding that the California law is preempted by the Federal Arbitration Act (FAA). What do employers need to know about AB 51 and what are the seven key takeaways from the 9th Circuit's ruling?

How Did We Get Here?

California Assembly Bill 51 would have made it unlawful for California employers to require applicants and employees to sign arbitration agreements as a condition of employment beginning January 1, 2020. Violations of the law could not only lead to civil and criminal penalties but would also be considered an "unlawful employment practice." This means they would have been subject to the private right of action under FEHA set forth in Government Code Section 12960, which could have open employers to retaliation claims associated with an employee's refusal to sign a mandatory arbitration agreement.

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At the time the law passed, we predicted that "the law could very well be blocked by a court before it ever takes effect" because "similar recent attempts at restricting arbitration have been struck down as conflicting with a strong federal law favoring it." As we reported, a coalition of business groups led by the U.S. Chamber of Commerce filed a lawsuit seeking to block AB 51 from ever taking effect.

Before January 1, 2020, a federal district court ultimately granted a preliminary injunction, which blocked AB51 from being enforced by the state while litigation continued on the merits. In September 2021, the 9th Circuit partially upheld and partially blocked the California law.

In another plot twist, the 9th Circuit decided to withdraw its prior ruling and rehear the case last year. That's what led to yesterday's ruling in which a three-judge panel for the 9th Circuit found that AB 51 is preempted by the FAA. Thus, the appeals court upheld the lower court's decision granting a preliminary injunction that blocks California's ban on mandatory arbitration.

7 Key Takeaways from Yesterday's Ruling

1. **Arbitration is Still Favored by Courts:** In its ruling yesterday, the 9th Circuit explained that AB 51 aimed to protect employees from "forced" arbitration. Notably, however, the FAA "embodies a national policy favoring arbitration," and under U.S. Supreme Court precedent, the FAA preempts state rules that discriminate against arbitration.

2. **Mixed Messages Caused Confusion:** To work around the federal policy favoring arbitration, according to the appeals court, California lawmakers only imposed criminal sanctions on employers for requiring an employee to enter into an arbitration agreement — whereas an executed agreement itself would still be enforceable. "This resulted in the oddity that an employer subject to criminal prosecution for requiring an employee to enter into an arbitration agreement could nevertheless enforce that agreement once it was executed," the federal appeals court observed. This created uncertainty for many employers when implementing arbitration agreements.

3. **Supreme Court Remains Supreme:** The court said California lawmakers "took this approach to avoid conflict

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with Supreme Court precedent" – but SCOTUS has clearly said that state rules burdening the formation of arbitration agreements are at odds with the FAA.

4. **Joining the Crowd:** The 9th Circuit joined the 1st Circuit and the 4th Circuit in finding that "the FAA preempts a state rule that discriminates against arbitration by discouraging or prohibiting the formation of an arbitration agreement."

5. **It's All or None:** Notably, the 9th Circuit found that all of AB51's provisions work together, and therefore, the appeals court declined to sever certain parts and uphold others.

6. **Federal Law Blocks California Law:** In conclusion, the 9th Circuit held that AB 51 is preempted by the FAA. In so ruling, the court concluded that the business groups are likely to succeed on the ultimate merits of their claim that the arbitration ban should be permanently blocked.

7. **Not the Final Nail in the Coffin – But Close:** Although a preliminary injunction only "temporarily" blocks the law while the court examines the underlying legality of the statute, the 9th Circuit's ruling that the FAA preempts AB 51 can essentially be read as a death knell for the state law. While the underlying litigation about the legality of the statute will still play out, the odds are overwhelmingly stacked towards AB 51 never seeing the light of day thanks to yesterday's ruling. California could also appeal this decision to the full 9th Circuit or even the U.S. Supreme Court, but again the final outcome does not appear at all hopeful for proponents of the statute. The California's Attorney General's office says they are "assessing" next steps in light of yesterday's ruling, so stay tuned for any future developments.

What Does This Mean for California Employers?

The 9th Circuit's ruling means that it's still lawful for most employers to continue requiring employees to sign arbitration agreements in California. But there are nuanced considerations that may limit this ability and vary by employer and industry. So, it's always best to have a conversation with competent employment counsel regarding these points and to ensure you have an up-to-date arbitration agreement.

Conclusion

We'll keep you posted on any additional legal developments, and you can stay updated on the latest news by making sure you are subscribed to Fisher Phillips' Insight System. For more information, contact your Fisher Phillips attorney, the authors of this Insight, or one of the attorneys in any of our California offices.