Legal Update Article

Federal Arbitration Act Partial Bar on California's Ban on Mandatory Arbitration Contracts, Court Holds

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The Federal Arbitration Act (FAA) only partially preempts California's bar on mandatory arbitration agreements in employment, the U.S. Court of Appeals for the Ninth Circuit has held, vacating the preliminary injunction that had been in place since early-2020 and enjoining enforcement of the law with respect to arbitration agreements governed by the FAA. *Chamber of Commerce of the U.S., et al. v. Bonta, et al*, No. 20-15291 (9th Cir. Sept. 15, 2021).

Background

In 2019, California passed Assembly Bill 51 (AB 51). AB 51 prohibits employers from requiring employees to sign arbitration agreements concerning disputes arising under the California Fair Employment and Housing Act (FEHA) or California Labor Code. Codified as California Labor Code section 432.6 and California Government Code section 12953, the law prohibits employers from conditioning employment or other employment-related benefits on an individual's consent to waive rights, forums, or procedures for alleged violations of the FEHA or the California Labor Code. It also prohibits employers from threatening, terminating, or otherwise retaliating or discriminating against employees or applicants because of their refusal to waive any rights, forums, or procedures for alleged FEHA or California Labor Code violations.

Early in 2020, as AB 51 took effect, a federal district court in California granted the U.S. Chamber of Commerce's request for a preliminary injunction, enjoining enforcement of AB 51 with respect to arbitration agreements governed by the FAA. The district court ruled AB 51 put arbitration agreements on an unequal footing with other contracts, in violation of the FAA, by imposing a higher consent requirement on arbitration agreements and potential civil and criminal penalties against employers seeking to enter into arbitration agreements. The State of California appealed the preliminary injunction to the Ninth Circuit.

Ninth Circuit Decision

A divided Ninth Circuit panel reversed, in part, the district court's order and vacated the district court's preliminary injunction. The Ninth Circuit concluded the FAA does not preempt AB 51 to the extent AB 51 seeks to regulate an employer's conduct *prior to executing an arbitration agreement* — for example, where an employer demands an individual sign an arbitration agreement. The Court held the FAA preempts AB 51 only to the extent AB 51 seeks to impose civil or criminal penalties on employers who have successfully executed arbitration agreements governed by the FAA.

In a vigorous dissent, Judge Sandra Ikuta distilled the logic and impact of the majority's decision:

> In case the effect of this novel holding is not clear, it means that if the employer

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> offers an arbitration agreement to the prospective employee as a condition of employment, and the prospective employee executes the agreement, the employer may not be held civilly or criminally liable. But if the prospective employee refuses to sign, then the FAA does not preempt civil and criminal liability for the employer under AB 51's provisions.
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> ...
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> This holding means that an employer's attempt to enter into an arbitration agreement with employees is unlawful, but a completed attempt is lawful. This tortuous ruling is analogous to holding that a statute can make it unlawful for a dealer to attempt to sell illegal drugs, but if the dealer succeeds in completing the drug transaction, the dealer cannot be prosecuted.

Next

As Judge Ikuta's dissent forecasts, the decision is unlikely to be the last word on the issue. The decision likely will be the subject of a petition for rehearing *en banc* to the Ninth Circuit, or for review by the U.S. Supreme Court.

Critically, the Ninth Circuit's decision does not immediately lift the preliminary injunction. The decision takes effect only when the Court issues its "mandate" and relinquishes jurisdiction over the case. A party has 14 days, subject to possible extension, to file a petition for rehearing or rehearing *en banc*. If such a petition is filed, issuance of the mandate is automatically stayed until the petition is decided. Otherwise, the Court will generally issue its mandate seven days after the deadline to file a petition for rehearing or rehearing *en banc* expires. Further, if a petition for review is filed with the U.S. Supreme Court, the U.S. Chamber of Commerce may move to stay issuance of the Ninth Circuit's mandate pending review by the high court. Therefore, it may be some time before the preliminary injunction is lifted, if ever.

Nevertheless, employers should closely monitor developments in this area and evaluate the options and risks associated with proceeding with mandatory employment arbitration agreements against the backdrop of AB 51.

Jackson Lewis attorneys will continue to track developments related to AB 51. If you have questions about how the Ninth Circuit ruling affects your business or about arbitration agreements, please contact a Jackson Lewis attorney to discuss.

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