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California's Arbitration Agreement Ban on Hold

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A controversial California law that would have prevented employers from requiring arbitration agreements as a condition of employment has been enjoined from taking effect by a federal district judge. Assembly Bill 51 (AB 51) was set to take effect last month, but the U.S. Chamber of Commerce, National Retail Federation, National Association of Security Companies, and several other trade organizations, challenged the statute, claiming it was preempted by the Federal Arbitration Act (FAA).

The FAA generally makes arbitration agreements "valid, irrevocable, and enforceable," and was expressly designed to reflect a national policy *favoring* arbitration. Under the FAA, a state may not pass or enforce laws that interfere with, limit, create unequal treatment of, or discriminate against arbitration.

Here, the district court on February 7, 2020, found that AB 51 did just that. The court found that both in its expressed purpose and its operation, AB 51 "singles out the requirement of entering into arbitration agreements and thus subjects these kind of agreements to unequal treatment." In issuing the injunction, the court agreed with the trade organizations that AB 51 would "forcefully impede the FAA's purpose 'to promote arbitration' by sanctioning employer behavior" connected to the formation of legally permissible arbitration

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agreements. Specifically, the court pointed to "the civil and criminal sanctions associated with violating the law," such as the potential exposure of up to six months' imprisonment or a fine up to $1,000 for employers who violate provisions of the California Labor Code, of which AB 51 would be a part. A law permitting penalties against employers for pursuing arbitration agreements, could hardly be said to "promote arbitration," the court noted. The preliminary injunction will remain in effect until the case is resolved.

Part of a Trend?

California is not the only state that has sought to bar mandatory arbitration agreements, nor the only one stopped on grounds of preemption. Just two years ago, the U.S. Supreme Court overturned an anti-arbitration decision from Kentucky's Supreme Court. There, the Kentucky court tried to invalidate arbitration agreements based on the state constitution's declaration of the right of court access and the "sacred" and "inviolate" nature of trial by jury. The U.S. Supreme Court overruled the state court's decision, reinforcing its longstanding precedent in favor of enforcing arbitration agreements under the FAA.

Nonetheless, several states have sought to limit the use of arbitration agreements. The #MeToo movement inspired a number of states to enact laws prohibiting companies from requiring arbitration of sexual harassment claims and similar claims, including Maryland, New York, Vermont, and Washington. Each has faced or will likely face a similar preemption challenge.

In the meantime, large employers should also be mindful of the potential cost of individual mandatory arbitration. Just last week, a California federal district court required a delivery service to individually arbitrate claims by more than 5,000 couriers. The couriers had all signed arbitration agreements, but when the American Arbitration

Association said the company owed about $12 million to start the cases, the company asked the court to stay arbitration until a pending class action was approved and couriers could decide whether to participate. The court rejected that plea with a stinging quote, “This hypocrisy will not be blessed.”

Whether California’s AB-51 is ultimately upheld remains to be seen, but for now mandatory arbitration agreements covered by the FAA in California live to see another day. Employers with questions about arbitration agreements should consult experienced labor and employment counsel.
