PAUL HASTINGS

Stay Current

February 2023

Follow @Paul_Hastings

The End of California's Anti-Arbitration Statute: Ninth Circuit Holds AB 51 is Preempted by the FAA

By Chris A. Jalian & Deisy Castro

Bringing an end to the saga of California's Assembly Bill 51, the Ninth Circuit Court of Appeals in *Chamber of Commerce v. Bonta*[1] has held, in a 2-1 decision, that the Federal Arbitration Act[2] preempts California's anti-arbitration statute, AB 51.

Background

AB 51, which was signed into law on October 10, 2019, invalidated attempts to form employer/employee arbitration agreements, in addition to imposing corresponding civil and criminal penalties on employers. This included making it a criminal offense for an employer to require, as a condition of employment, that an existing employee or a job applicant sign an agreement to arbitrate claims under the California Fair Employment Housing Act or California Labor Code. AB 51 also precluded an employer from refusing to hire any applicant or discharging any employee for declining to sign an arbitration agreement, even where the agreement would have been governed by the FAA.

In December 2019, business and trade organizations challenged AB 51 as preempted by the FAA and sought to enjoin the State from enforcing it. Soon after, in February 2020, the District Court granted a preliminary injunction against enforcement of AB 51 after it concluded the Plaintiffs were likely to succeed on their claim that the FAA preempts AB 51.[3] The State appealed and, in September 2021, the Ninth Circuit panel, 2-1, reversed the District Court's injunction, and held that the FAA does not preempt AB 51.[4] Following a rehearing petition, one judge in the majority joined the originally dissenting judge and agreed to reconsider the case from scratch.[5]

The Ninth Circuit's Opinion

On February 15, 2023, the Ninth Circuit affirmed the District Court's preliminary injunction and held that Supreme Court precedent teaches that the FAA preempts AB 51.

The California legislature had attempted to avoid FAA preemption by including language in AB 51 that allowed for the legal enforcement of arbitration agreements once executed. "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."[6] But, as the Court explained, the Supreme Court "has made clear that the FAA's preemptive scope 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."[7] Otherwise, a state could defeat the FAA's purpose by criminalizing the act of entering into an arbitration agreement.

Thus, and in agreement with decisions from the First and Fourth Circuit Courts of Appeals, the Ninth Circuit held that "the FAA preempts a state rule that discriminates against arbitration by discouraging or prohibiting the formation of an arbitration agreement."[8] Given the severity of AB 51's penalty scheme, AB 51 deters employers from including non-negotiable arbitration requirements in employment agreements by imposing civil and criminal penalties. As such, AB 51 is hostile towards arbitration, something that the FAA forbids.

The majority rejected the State's argument, as well as the argument in Judge Lucero's dissent (and in his prior September 2021 opinion), that AB 51 merely prohibits "forced arbitration" by requiring employees to voluntarily consent to arbitration provisions. The Court found this argument meritless because, under California law, an employee can "consent" to an employment agreement, even if the agreement contains terms the employee dislikes or is the product of unequal bargaining power, so long as it is not invalid due to generally applicable contract principles, like unconscionability. As such, employees can consent to an arbitration agreement, even if they are required to sign such an agreement as a condition of employment, so long as the agreement is otherwise enforceable.

What This Means for Employers

FAA-covered California employers may continue to require their employees and job applicants to sign arbitration agreements as a condition of employment. One important reason to do so is to obtain lawful class action waivers, which can be made expressly,[9] but are also implicit in arbitration agreements that are silent or ambiguous on the issue.[10]

Employers who wish to obtain new arbitration agreements, either for new hires or incumbents, should first ensure that the FAA applies. Notably, the FAA does not apply:

1. to exceptionally small employers, where no nexus to interstate commerce exists;[11]
2. to certain transportation workers, to whom the FAA by its terms does not apply;[12] and
3. to arbitration agreements that lawfully (but unwisely) invoke state arbitration law instead of the FAA.[13]

If the FAA applies, employers interested in commencing an arbitration program should consider whom to cover, and how to do it. New hires can be required to enter into arbitration contracts as a condition of hire. Incumbent employees can also be covered through various types of arbitration agreements, such as so-called "quit, or you're bound" agreements, "opt out" agreements, or agreements tied to promotion offers. Nevertheless, given that arbitration agreements are subject to challenge if not put in place carefully, employers should consult with legal counsel before proceeding.

✧ ✧ ✧

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

Los Angeles

Elena R. Baca
1.213.683.6306
elenabaca@paulhastings.com

Chris A. Jalian
1.213.683.6143
chrisjalian@paulhastings.com

Deisy Castro
1.213.683.6178
deisycastro@paulhastings.com

San Francisco

Ryan D. Derry
1.415.856.7092
ryanderry@paulhastings.com

Zach P. Hutton
1.415.856.7036
zachhutton@paulhastings.com

---

[1] *Chamber of Com. of the United States of Am. v. Bonta*, No. 20-15291, __ F.4th __, 2023 WL 2013326 (9th Cir. Feb. 15, 2023).

[2] 9 U.S.C. § 1 *et seq.*

[3] *Chamber of Com. of United States v. Becerra*, 438 F. Supp. 3d 1078 (E.D. Cal. 2020).

[4] *Chamber of Com. of United States v. Bonta*, 13 F.4th 766, 771 (9th Cir. 2021).

[5] *Chamber of Com. of United States v. Bonta*, 45 F.4th 1113 (9th Cir. 2022)

[6] 2023 WL 2013326, at *4.

[7] *Id.* at *7 (citing *Kindred Nursing Centers Ltd. P'ship v. Clark*, __ U.S.__, 137 S. Ct. 1421, 1428-29 (2017); *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 683 (1996)).

[8] *Id.* at *8 (citing *Saturn Distribution Corp. v. Williams*, 905 F.2d 719, 723 (4th Cir. 1990); *Sec. Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1123-24 (1st Cir. 1989)).

[9] *See, e.g., AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 336 (express class waiver).

[10] *Lamps Plus, Inc. v. Varela*, __ U.S. __, 139 S. Ct. 1407, 1415, 1419 (2019) (an agreement silent or ambiguous on the availability of a class action cannot be construed to allow it).

[11] The FAA's test for interstate commerce often is easily met. For example, the Supreme Court found that the FAA applies to a contract for termite-eradication services in a single dwelling. *See Allied-Bruce Terminex Cos. v. Dobson*, 513 U.S. 265, 273-75 (1995).

[12] 9 U.S.C. § 1; *see Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 109, 119 (2001) (construing narrowly the transportation-worker exception).

[13] *See Volt Info. Scis. v. Bd. of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 470, 477-79 (1989) (contracts lawfully may opt out of FAA coverage).