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Ninth Circuit Ruling On AB 51 Means That Mandatory Arbitration Agreements Are Now Prohibited In California

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On September 15, 2021, the Ninth Circuit Court of Appeals held in *Chamber of Commerce v. Bonta* that the Federal Arbitration Act ("FAA") does **not** fully preempt California Assembly Bill 51 ("AB 51"), reversing a lower court ruling holding that AB 51 was preempted by the FAA. As a result, employers are now prohibited from requiring applicants and employees in California to enter into mandatory arbitration agreements as a condition of employment.

AB 51—which added Section 432.6 to the California Labor Code—prohibits employers from requiring employees and applicants to waive any right, forum, or procedure, including the right to file a civil action or complaint, as a condition of employment or continued employment. Requiring an employee to opt out of arbitration is also deemed an impermissible condition of employment. A violation of Section 432.6 is a criminal misdemeanor under the Labor Code that can subject an employer to potential civil and criminal penalties, including up to six months in jail. AB 51 was first passed in October 2019 and was to become effective on January 1, 2020. However, U.S. District Court judge Kimberly Mueller issued a TRO on December 28, 2019, followed by a Preliminary Injunction on January 31, 2020 against the State of California, enjoining the State from enforcing AB 51 on the grounds the California statute was preempted by the FAA (as previously reported by Vedder here).

In a 2-1 decision, however, the Ninth Circuit in *Bonta* reversed in part and lifted the stay on enforcement. The two judges in the majority concluded that because AB 51 was focused on the conduct of the employer **prior to** entering into an arbitration agreement, the statute did not conflict with the FAA and the State was free to regulate that conduct and prohibit employers from requiring mandatory arbitration as a condition of employment. Accordingly, pursuant to Labor Code Section 432.6, employers cannot seek to require California applicants and employees to enter into mandatory arbitration agreements as a condition of employment. However, AB 51 does **not** void any arbitration agreements previously entered into under the FAA, does **not** prohibit employers from offering arbitration on a voluntary basis and, strangely, does **not** void or render unenforceable an arbitration agreement signed by any person going forward under the FAA, even if the agreement had been required as a condition of employment.

Notably, in a very strange ruling, the Ninth Circuit majority concluded that if the employee does in fact sign the arbitration agreement, then not only is the agreement valid and enforceable under the FAA (and AB 51), but the criminal and civil penalties that otherwise would be available for violations of Section 432.6 are preempted by the FAA and cannot be enforced by the State against the employer. This creates the bizarre situation that if the employer offers an arbitration agreement 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** the agreement, then the FAA does not preempt AB 51 and the employer can face civil and criminal liability for having presented the agreement as a condition of employment.[1]

Judge Ikuta in dissent noted that the majority's ruling conflicted with the Supreme Court's clear guidance in *Kindred Nursing Centers Ltd. Partnership v. Clark*, 137 S. Ct. 1421, 1425 (2017), which held that the FAA invalidates state laws that impede the formation of arbitration agreements. Judge Ikuta also agreed with Judge Mueller of the District Court in noting

[1] Judge Ikuta in his dissent summarized the situation as follows: "In other words, the majority holds that if the employer successfully 'forced' employees 'into arbitration against their will,'… the employer is safe, but if the employer's efforts fail, the employer is a criminal."

that AB 51's civil and criminal penalties stood as an obstacle to the purposes of the FAA and therefore AB 51 was preempted by the FAA. The decision also created a circuit split with the First and Fourth Circuits, which have issued contrary rulings in other contexts dealing with pre-agreement restrictions. Accordingly, it is anticipated that further appeals to the full Ninth Circuit or Supreme Court may follow.

In the interim, this decision places employers on notice to review their practices regarding arbitration agreements for employees in California to avoid potential liability. Please contact Vedder Price attorney **Thomas H. Petrides** at tpetrides@vedderprice.com, **Osaama Saifi** at osaifi@vedderprice.com, **Lauren E. Wertheimer** at lwertheimer@vedderprice.com or any other Vedder Price California attorney with whom you work, to determine whether your practices and arbitration agreements are in compliance with this new change in the law.