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Ninth Circuit Holds that AB 51 is Preempted

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On February 15, 2023, the U.S. Court of Appeals for the Ninth Circuit ruled in *Chamber of Commerce v. Bonta* that California's Assembly Bill 51 ("AB 51") is preempted by the Federal Arbitration Act (FAA). After two failed attempts to pass similar legislation in 2015 and 2018, the California legislature passed AB 51 in 2019, but the bill was promptly challenged and enjoined by the Eastern District of California on the basis that it was preempted by the FAA, among other reasons. AB 51 would have made it a crime for employers to require employees to sign arbitration agreements as a condition of employment but would not have prohibited employers from enforcing agreements signed in violation of the law. This paradoxical result was the product of the legislature's attempt to avoid FAA preemption.

The Supreme Court of the United States has repeatedly made it clear that the purpose of the FAA is to promote arbitration. On numerous occasions, the Supreme Court has struck down laws that discriminate against or disfavor arbitration agreements on preemption grounds. When it enacted AB 51, the California legislature attempted to evade preemption by focusing on the formation stage of the arbitration agreement, rather than the enforcement stage. The legislature argued that AB 51 was not preempted because it did not prevent employers and employees from agreeing to arbitrate disputes; it only prevented employers from compelling employees to arbitrate. On September 15, 2021, the Ninth Circuit issued an opinion siding with the legislature. However, following the Supreme Court's decision in Viking River Cruises, Inc. v. Moriana, the panel announced that it would reconsider the decision.

Following reconsideration, the Ninth Circuit rejected the legislature's argument, noting that the statute clearly disfavored arbitration agreements and imposed a severe burden on their formation. Strictly speaking, the law did not apply exclusively to arbitration agreements. It prohibited agreements requiring employees to waive any "forum or procedure." However, it was clear from the legislative history that arbitration was the primary focus of AB 51 and the law imposed an obstacle on executing arbitration agreements that did not apply to other types of agreements. The court observed that California courts generally permit employers to enter into agreements with employees concerning non-negotiable terms of employment, such as requirements concerning compensation or drug use. Singling out arbitration agreements would be "antithetical" to the FAA's policy favoring arbitration, the court said.

The court also found no merit to the legislature's argument that AB 51 was needed to protect employees against "forced arbitration," which the court characterized as a misunderstanding of the basic principles of California contract law. The court noted that the FAA does not prevent parties to arbitration agreements from challenging their enforceability based on generally applicable contract defenses, such as unconscionability, duress, or circumstances negating mutual assent. Accordingly, it was not necessary for the legislature to enact AB 51 to protect employees from overreaching agreements.

Further, because AB 51 applied to all arbitration agreements, the legislature's argument that AB 51 regulated only unconscionable arbitration agreements, amounted to an argument that all employment-related arbitration agreements are unconscionable, which was precisely the type of hostility the FAA

was enacted to prevent.

Although the Ninth Circuit's decision may be welcome news to employers who desire to arbitrate employment disputes, history suggests that AB 51 will not be the legislature's final attempt to undermine the FAA. Employers should continue to closely monitor legislative developments concerning arbitration agreements. Additionally, in light of the Ninth Circuit's reminder, employers should consider consulting with counsel to confirm that their arbitration agreements are not vulnerable to challenges based on unconscionability or other generally applicable contract defenses.