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WSHB EMPLOYMENT ALERT: CALIFORNIA LAW BANNING ARBITRATION AGREEMENTS TEMPORARILY ON HOLD

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On October 10, 2019, California Governor Gavin Newsom signed a law prohibiting employers from requiring employees to sign arbitration agreements as a condition of employment on or after January 1, 2020. The law, AB 51, expressly prohibits companies from compelling employees to waive any right, forum or procedure for a violation of any provision of the California Labor Code or Fair Employment and Housing Act, and puts employers who violate the law at risk of being found guilty of a misdemeanor.

Various interested business groups, including the United States Chamber of Commerce (Plaintiffs) filed suit in the United States District Court for the Eastern District of California challenging the new law on several grounds, requesting a preliminary injunction on the grounds that the law was preempted by the Federal Arbitration Act ("FAA"). On December 29, United States District Judge Kimberly J. Mueller issued a temporary restraining order ("TRO") preventing the law from taking effect on January 1, 2020. The court was concerned about whether the FAA, as construed by the United States Supreme Court in prior cases, preempted AB 51, and also about allowing the statute to take effect, even briefly, which may negatively impact the validity or enforceability of standard form employment contracts.

On January 10, 2020, the Court held a hearing on the preliminary injunction. Before the hearing, we anticipated one of two outcomes: (1) the preliminary injunction would be granted and the law would be further delayed from going into effect, if ever; or (2) the preliminary injunction would be denied and the law will go into effect pursuant to the Court's order, with some restrictions. We were optimistic that option 1 would be the likely outcome, based on the Court's ruling on the TRO in which it stated, "plaintiffs have raised serious questions regarding whether the new law is preempted by [federal law] as construed by the United States Supreme Court." It also noted that Plaintiff's "argument that allowing the statute to take effect even

briefly, if it is preempted, will cause disruption in the making of employment contracts is also persuasive."

Further proceedings on the preliminary injunction were held on January 10, 2020, and after hearing arguments from Plaintiffs (business groups challenging the law) and the California Attorney General (defending the law), Judge Mueller ordered a supplemental briefing from the parties on several issues, including the parties' positions about severability of portions of the law if the Court grants the business groups' motion for a preliminary injunction "at least in part." That briefing is under way. If Judge Mueller finds that portions of the law are severable, she could enforce some provisions of the law, while finding others are not enforceable. Judge Mueller also ruled that, pending the Court's ruling on the motion for a Preliminary Injunction, that the TRO remains in effect until January 31, 2020; however, the Court modified the order to clarify that the State of California is enjoined from enforcing the law "to the extent it applies to arbitration agreements covered by the Federal Arbitration Act (FAA)."

What does this mean for California employers? If an employment agreement or company policy requires an employee to sign an arbitration agreement, so long as it requires arbitration under the FAA, the Agreement should withstand a legal challenge—for now. For other agreements that don't require arbitration under the FAA (applying other rules like the AAA, or JAMS), existing agreements should be reviewed and modified to ensure they are governed by the FAA. Even if an arbitration agreement currently does not require arbitration under the FAA, its unlikely that a legal challenge will be successful while AB 51 is under such intense scrutiny and works its way through the federal court system.

A final ruling on the preliminary injunction should be made in the next several weeks and the most logical step would be to adopt the FAA rules and incorporate it into existing arbitration agreements. In the worst case scenario, if a preliminary injunction is denied and AB 51 becomes enforceable, modifying current arbitration agreements to ensure they are truly voluntary in nature, and not a mandatory condition of employment, should render them enforceable going forward.

We will continue to monitor further developments in this case and report on them as they become available.