Ninth Circuit Blocks Controversial AB 51

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Following three years of legal challenges, the Ninth Circuit Court of Appeals again weighed in on California's controversial Assembly Bill 51 ("AB 51"), which prohibited employers from forcing employees to enter into arbitration agreements as a condition of employment. In a win for employers, the Ninth Circuit, in *Chamber of Commerce of the U.S., et al. v. Bonta, et al.*, declared in a 2-1 decision that AB 51 was preempted by the Federal Arbitration Act ("FAA").

Background

AB 51 was certain to face legal challenges from the moment Governor Newsom signed it into law in 2019. Among other things, AB 51 made it unlawful for employers to require employees to agree to arbitrate employment claims as a condition of employment, even if the arbitration agreement contained an opt-out clause. The law subjected employers to civil and criminal penalties for any violations. AB 51 also opened up employers to unfair business practice and retaliation claims stemming from an employee or applicant refusing to sign a mandatory arbitration agreement.

On the eve of AB 51 taking effect in 2020, a federal district court in California enjoined enforcement at the request of the coalition of business groups, including the U.S. Chamber of Commerce. After the State appealed, the same three-judge Ninth Circuit panel in 2021 vacated the preliminary injunction and upheld portions of AB 51, setting the stage for an *en banc* hearing (a full panel of Ninth Circuit judges rather than a three-judge panel).

But following the United States Supreme Court's 2022 decision in *Viking River Cruises, Inc. v. Moriana*, which addressed a related issue concerning arbitration and the California Private Attorneys General Act ("PAGA"), the Ninth Circuit took the surprising step of withdrawing its 2021 ruling and rehearing the AB 51 challenge.

The Ruling

In a divided 2-1 decision, the same Ninth Circuit panel — citing the national policy favoring arbitration under the FAA — held that AB 51 was preempted by the FAA because it placed obstacles to the formation of arbitration agreements. The panel noted that AB 51 was specifically drafted to avoid conflict with Supreme Court precedent, echoing the dissent from its 2021 ruling that the law was a "transparent effort to sidestep" the FAA.

The Ninth Circuit panel similarly took issue with AB 51's unique penalty scheme that imposed criminal sanctions on employers who required an employee enter into an arbitration agreement, while simultaneously deeming the executed agreement enforceable. The panel commented, "[t]his 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."

The majority also reaffirmed longstanding principles regarding the execution of employment

contracts, stating that “under California law, an employee can ‘consent’ to an employment contract by entering into it, even if the contract was a product of unequal bargaining power and even if it contains terms (such as an arbitration provision) that the employee dislikes, so long as the terms are not invalid due to unconscionability or other generally applicable contract principles.”

Finally, the majority rejected California’s argument that clauses violative of the FAA could be severed from AB 51, leaving the remainder intact. The panel explained that because all of the clauses of AB 51 work together and in concert, there was no way it could be severed and survive as constructed.

What Now?

While this is likely the end of AB 51, California may try to seek *en banc* review, though doing so may not change the outcome given that, as noted by the majority opinion, at least two other Circuits have struck down similar laws preventing parties from entering into arbitration agreements. And, even if a full Ninth Circuit panel were to reverse course and uphold the enforceability of AB 51, the current U.S. Supreme Court would likely strike it down again.

In response to the ruling, employers are in the clear to resume (or initiate) mandating arbitration agreements as a condition of employment (with or without opt-out clauses), subject to ordinary contract principles and defenses.

Haynes Boone will continue to monitor any developments related to AB 51. Please contact the authors of this post or your Haynes Boone attorney should you have any questions or would like to discuss the enforceability of your arbitration agreements.