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Arbitration changes in 2020

UNDERSTANDING THE TWO EMPLOYMENT AND CONSUMER ARBITRATION BILLS SIGNED INTO LAW IN 2019

Last year, Governor Gavin Newsom signed into law two arbitration-related bills, AB 51 and SB 707. Both are summarized and analyzed below.

SB 707 has been in effect since January 1, 2020. While AB 51 was supposed to take effect the same day, it has already been challenged by business organizations. As discussed in more detail below, a coalition of business organizations – led by the U.S. Chamber of Commerce – filed suit on December 9, 2019, seeking to enjoin AB 51 as preempted by the Federal Arbitration Act. (*Chamber of Commerce of the United States et al. v. Becerra et al.*, No. 2:19-cv-02456 (E.D. Cal.).)

On December 30, 2019 – just two days before AB 51 was scheduled to go into effect – the United States District Court of the Eastern District of California issued a temporary restraining order blocking AB 51's enforcement. On January 10, 2020, the same court will hear a motion for a preliminary injunction. If granted, AB 51 will be enjoined throughout the pendency of the litigation. As of now, California is temporarily enjoined from enforcing AB 51.

This article was sent to the publisher before January 10, 2020, the date when the court will hear the motion for a preliminary injunction. Even if the court does not grant a preliminary injunction and even if the business organizations do not prevail in the above-mentioned litigation, the inevitable challenges to AB 51 will continue. (*Editor's Note: The court kept the injunction in place.*)

Thus, in addition to discussing SB 707, this article will help plaintiffs' employment lawyers educate themselves (and potentially judges in the future) how business organizations are completely misguided in arguing that AB 51 is preempted by the Federal Arbitration Act.

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SB 707's amendments to the Code of Civil Procedure

SB 707 amends Sections 1280 and 1281.96 of the Code of Civil Procedure, and adds Sections 1281.97, 1281.98, and 1281.99 to, the Code of Civil Procedure.

The problem SB 707 was enacted to address

SB 707 was much needed because California law was previously *silent* on what employees and consumers could do if companies failed to pay arbitration fees. Under the Federal Arbitration Act ("FAA"), courts can declare a party to be in "default of arbitration."

However, the FAA does *not* grant non-defaulting parties the remedies typically available in a judicial proceeding. Moreover, the FAA does *not* directly address the scenario(s) in which a party breaches the arbitration agreement. The California Arbitration Act is even less instructive, providing no guidance at all to parties or arbitration companies (e.g., Signature, AAA, JAMS). *But now*, SB 707 provides the procedural remedy for consumers and employees when companies strategically withhold payment of arbitration fees in order to stall or impede arbitration proceedings.

SB 707 was much needed not only conceptually, but in practice. To combat the statistically pro-employer arbitration process, lawyers representing consumers and employees have increasingly resorted to the activist strategy of filing thousands of individual arbitrations against companies like Uber, Lyft, DoorDash and Postmates. This activist strategy hit the companies with millions of dollars in arbitration-related fees. Companies one by one refused to pay arbitration fees and costs in response. Since more and more companies have statistically been refusing to pay arbitration fees as a litigation strategy, SB 707 was passed to reverse that trend.

Lastly, SB 707 also requires arbitration companies to now disclose arbitrators' demographic data (namely gender, race/ethnicity, sexual orientation, gender identity, and veteran and disability status). The Legislature noted that the Judicial Council of California was already tracking its commitment to increasing diversity in our justice system. Government Code section 12011.5, subdivision (n) requires the Judicial Council of California to collect and release aggregate demographic data of California state court justices and judges, by specific jurisdiction each calendar year. No similar reporting requirement existed for arbitration companies until SB 707 became effective on January 1, 2020.

Summary of SB 707

This new law applies to employment or consumer arbitration agreements and imposes stiff penalties on businesses that stall payments beyond 30 days of their due date; *one such "penalty" is that employees or consumers may elect to withdraw their claim from arbitration and proceed in court*. (Code Civ. Proc., §§ 1281.97, subd. (b)(1), 1281.98, subd. (b)(1).)

If a company or business fails to timely pay arbitration fees and costs, SB 707 *explicitly* states that it is in default of the arbitration and has waived its right to compel arbitration. In this scenario, SB 707 outlines *four* procedural remedies available to employees and consumers:

First, they may elect to withdraw the claim from arbitration and proceed in court. (Code Civ. Proc. §§ 1281.97, subd. (b)(1), 1281.98, subd. (b)(1).);

Second, they may pay the employer's unpaid fees in order to continue the arbitration, and recover the amount paid at the end of the proceeding regardless of whether or not they prevail in arbitration. (Code Civ. Proc. § 1281.98, subd. (b)(4).);

Third, they may petition the court for an order compelling the employer to pay the arbitration fees (Code Civ. Proc. § 1281.98, subd. (b)(3).);

Finally, they may choose to continue in arbitration, provided that the arbitration company agrees to continue as well. (Code Civ. Proc. § 1281.98, subd. (b)(2).)

In enacting SB 707, the Legislature explicitly affirmed the decisions in *Armendariz v. Foundation Health Psychcare Services, Inc., Brown v. Dillard's, Inc.*, and *Sink v. Aden Enterprises, Inc.* for the propositions that a company's failure to pay arbitration fees pursuant to a mandatory arbitration provision constitutes a breach of the arbitration agreement and allows the non-breaching party to bring a claim in court. The Legislature specifically noted that:

In *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, the California Supreme Court concluded that "when an employer imposes mandatory arbitration as a condition of employment, the arbitration agreement or arbitration process cannot generally require the employee to bear any type of expense that the employee would not be required to bear if he or she were free to bring the action in court."

In *Brown v. Dillard's, Inc.* (2005) 430 F.3d 1004, the Ninth Circuit held that, under federal law, an employer's refusal to participate in arbitration pursuant to a mandatory arbitration provision constituted a breach of the arbitration agreement.

In *Sink v. Aden Enterprises, Inc*. (2003) 352 F.3d 1197, the Ninth Circuit held that, under federal law, an employer's failure to pay arbitration fees as required by an arbitration agreement constitutes a material breach of that agreement and results in a default in the arbitration.

Again, SB 707 also addresses the issue of diversity in the arbitration industry by requiring arbitration companies to report the same kind of demographic information about their arbitrators as the Judicial Council is required to report about state court justices and judges. The arbitration companies hopefully will decide not to reinvent the wheel and will model their demographic data disclosures like the Judicial Council does. By way of example, Judicial Council demographic data between 2007 and 2019 is available at: https://www.courts.ca.gov/13418.htm.

After a company's failure to pay arbitration fees: the first option available

Statute of limitations is tolled back to the date of the first filing

If a consumer or employee exercises the option to proceed in court, the statute of limitations "with regard to all claims

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brought or that relate back to any claim brought in arbitration shall be tolled as of the date of the first filing of a claim in any court, arbitration forum, or other dispute resolution forum." (Code Civ. Proc., §§ 1281.97, subd. (c), 1281.98, subd. (b)(1).)

Available remedies (e.g., sanctions) if consumer/employee elects to proceed in court

If the employee or consumer proceeds with an action in a court after a company fails to timely pay arbitration fees, "*both* of the following apply": (1) "The employee or consumer may bring a motion, or a separate action, to recover all attorney's fees and all costs associated with the abandoned arbitration proceeding. The recovery of arbitration fees, interest, and related attorney's fees shall be without regard to any findings on the merits in the underlying action or arbitration" (Code Civ. Proc., §§ 1281.97, subd. (d), 1281.98, subd. (c)(1)); *and* (2) the court "*shall* impose sanctions." (Code Civ. Proc., §§ 1281.97, subd. (d), 1281.98, subd. (c)(2) (emphasis added).

With respect to the latter "sanctions," the court *must* "impose a *monetary* sanction" against the company by ordering the company "to pay the reasonable *expenses, including attorney's fees and costs*, incurred by the employee or consumer." (Code Civ. Proc., § 1281.99, subd. (a) (emphasis added).

The court *may* also order various other possible sanctions "unless the court finds that one subject to the sanction acted with substantial justification or that other circumstances make the imposition of the sanction unjust." (Code Civ. Proc., § 1281.99, subd. (b) (emphasis added).) The following are *enumerated* examples of possible non-monetary sanctions that the court *may* award:

"An evidence sanction" prohibiting the company "from conducting discovery in the civil action" (Code Civ. Proc., § 1281.99, subd. (b)(1).);

"A terminating sanction…striking out the pleadings or parts of the pleadings" (Code Civ. Proc., § 1281.99, subd. (b)(2)(A).);

"A terminating sanction" rendering a default judgment (Code Civ. Proc. § 1281.99(b)(2)(B));

"A terminating sanction" treating the company "as in contempt of court." (Code Civ. Proc., § 1281.99, subd. (b)(2)(C).)

Other options available pursuant to SB 707

Same remedies available for all other options

To recap, an employee or consumer has four possible options in the event a company fails to timely pay arbitration fees. One option (exhaustively discussed above) is to withdraw from arbitration and proceed in court.

All three remaining options are applicable when an employee or consumer decides to remain in arbitration (and does *not* elect to proceed in court). (Code Civ. Proc., § 1281.98, subd. (d).) *With respect to all three remaining options, the remedy is the same*: "the *arbitrator shall* impose *appropriate* sanctions…including monetary sanctions, issue sanctions, evidence sanctions, or terminating sanctions." (Code Civ. Proc., § 1281.98, subd. (d).)

Thus, the arbitrator arguably has more leeway in deciding what remedies to order compared to the ones available should the employee or consumer elect to go to court. To be clear, regardless of whether the employee or consumer elects to go back to court or stay in arbitration, both the court and arbitrator *must* sanction a company for not timely paying arbitration fees.

However, the remedies are arguably more explicit should the employee or consumer elect to go to court. In such a scenario, a court *must* grant monetary sanctions but can refuse to grant any additional non-monetary sanctions by finding that a company acted with "substantial justification." (Code Civ. Proc., § 1281.99, subds. (a)-(b) (emphasis added). While the arbitrator *also must* sanction a company for not timely paying arbitration fees, he or she has arguably unfettered discretion in deciding what sanctions(s) are "appropriate." (Code Civ. Proc., § 1281.98, subd. (d).) For example, an arbitrator can order terminating sanctions but find that it is not "appropriate" to award an employee or consumer monetary sanctions (such as fees and costs).

The remaining three options if a company does not timely pay arbitration fees (all involve staying in arbitration)

First, the employee or consumer may elect to pay the company's unpaid fees and continue litigating in arbitration. If this option is chosen, the arbitration award *must* provide for the recovery of all arbitration fees paid by the employee or consumer regardless of whether or not the employee or consumer prevails during the arbitration hearing. (Code Civ. Proc., § 1281.98, subd. (b)(4) (emphasis added).

Second, the employee or consumer may continue litigating in arbitration but also petition the court to compel the company to pay all arbitration fees that the company "is obligated to pay under the arbitration agreement or the rules of the arbitration company." (Code Civ. Proc., § 1281.98, subd. (b)(3).)

Third and finally, if the company fails to timely pay arbitration fees, the employee or consumer may continue litigating in arbitration (as long as the arbitration company agrees to continue without being paid). SB 707 gives arbitration companies a remedy if they agree to proceed with the arbitration without being paid their fees (namely instituting a collection action against the drafting party for all fees and costs). (Code Civ. Proc., § 1281.98, subd. (b)(2).)

If the last option is chosen, recall that the employee or consumer has a remedy as well where "the arbitrator *shall* impose *appropriate* sanctions…including monetary sanctions, issue sanctions, evidence sanctions, or terminating sanctions." (Code Civ. Proc., § 1281.98, subd. (d).)

AB 51 did not become effective Jan. 1 as intended

As discussed in the introduction above, the court in *Chamber of Commerce of the United States et al. v. Becerra et al.*, No. 2:19-cv-02456 (E.D. Cal.) issued a temporary restraining order blocking AB 51's enforcement on December 30, 2019. (The court kept the injunction in place – editor.)

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Where AB 51 would be codified

AB 51 would add Section 432.6 to the Labor Code and Section 12953 to the Government Code.

Why businesses are fighting so hard against AB 51

AB 51 would make it unlawful for employers to impose arbitration agreements on employees as a condition of employment, even if employees are permitted to opt out. (Lab. Code, § 432.6, subds. (a), (c).) AB 51 would also prohibit employers from threatening, retaliating against, or discriminating against employees or applicants for refusing to waive their rights, "including the right to file and pursue a civil action or a complaint" for a violation of the California Fair Employment and Housing Act ("FEHA") or the California Labor Code. (Lab. Code, § 432.6, subd. (b).) It would be a *criminal* misdemeanor for an employer to violate AB 51.

Scenarios where AB 51 would be applicable

AB 51 would apply to arbitration agreements "entered into, modified, or extended on or after January 1, 2020." (Lab. Code, § 432.6, subd. (h).) The word "extended" is *not* to be used in an attempt to invalidate signed arbitration agreements entered into or modified *before* January 1, 2020. In other words, AB 51 does not create a right to rescind an arbitration agreement entered into or modified *before* January 1, 2020 if an employer is simply attempting to enforce that agreement.

Misguided arguments by businesses

The coalition of business organizations is completely misguided in the arguments being made to the Eastern District of California. In *Chamber of Commerce of the United States et al. v. Becerra et al.*, No. 2:19-cv-02456 (E.D. Cal.), the business organizations are trying to convince the court that AB 51 is preempted by the Federal Arbitration Act ("FAA"). Even if the Eastern District of California ultimately disagrees with them, there will likely be some other inevitable challenge to AB 51. Thus, plaintiffs' employment lawyers should familiarize themselves as to exactly why the business organizations are so misguided.

Template brief

Below is a (quick and dirty) long-form rough version of a **template brief** that advocates of AB 51 can pick and choose from to educate themselves (and judges) as to exactly why business organizations are completely misguided when arguing that AB 51 is preempted by the FAA.

Summary of the dispute at issue

The legal question at issue is simply whether an employer can require applicants and current employees to waive their right to go to court and to other workplace protections as a condition of employment in the face of AB 51 (a state law providing that all such waivers are unlawful).

The Federal Arbitration Act ("FAA") does not govern contract formation, so AB 51 cannot possibly be preempted by the FAA. AB 51 fully preserves an employer's ability to request arbitration – it simply prohibits the employer from retaliating against a potential employee for refusing to agree. Since a contract is not formed, federal law protecting contracts does not come into play.

AB 51 does not prohibit, restrict, or discourage anyone from entering into a mandatory arbitration agreement, if they wish to consent to do so freely and voluntarily. It does not interfere with enforcement of arbitration agreements. An employer that believes arbitration lowers the cost of resolving employment-related disputes can make arbitration available to employees who wish to avail themselves of that option. Such an employer will remain free to advertise the advantages of arbitration among its prospective and current employees. Doubtlessly, some employees will choose to agree to arbitration. In other words, employers may maintain a system of arbitration to resolve workplace disputes and make that system available to employees who may agree to arbitrate disputes.

In fact, once a mandatory arbitration agreement has been signed, AB 51 has nothing more to say about the situation. In short, nothing in AB 51 discriminates against arbitration and nothing in AB 51 interferes with the enforcement of an agreement to arbitrate once executed.

The FAA is inapplicable because California law governs the formation of contracts

The FAA does not regulate contract formation. In fact, the United States Supreme Court has explicitly recognized that in applying the FAA, courts "should apply ordinary state law principles that govern formation of contracts." (*First Options of Chicago, Inc. v. Kaplan* (1995) 514 U.S. 938, 944; see also *AT&T Mobility LLC v. Concepcion* (2011) 563 U.S. 333, 347 n.6 ("Of course States remain free to take steps addressing the concerns that attend contracts of adhesion.").

Thus, California law governs formation of contracts. The California state legislature can impose conditions to determine when such agreements are so unfair that they are unenforceable, and it has done so (e.g., finding agreements unenforceable because of duress). AB 51 is a proper exercise of this state function.

AB 51 is consistent with the congressional intent behind the FAA

AB 51 also cannot possibly be preempted by the FAA in part because it does not disfavor arbitration, which is the congressional intent behind the FAA. Rather, AB 51 simply represents a finding on the part of the California legislature that it is unfair for employers to condition employment on a waiver of any of the rights contained in the FEHA or the Labor Code. That protection is consistent with established Supreme Court jurisprudence. (See *Brooklyn Savings Bank v. O'Neil* (1945) 324 U.S. 697, 707 ("policy considerations . . . forbid waiver of basic minimum and overtime wages").

Just as employers cannot condition employment on waiving the right to basic minimum wage or premium pay for overtime work or the right to be free from discrimination, AB 51 simply declares

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employers should not be able to condition employment on waiving the rights contained in the FEHA or the Labor Code.

Striking down AB 51 would contradict prior guidance from the U.S. Supreme Court

Striking down AB 51 would treat forced agreements to arbitrate *more* favorably than forced agreements to waive all other rights contained in the FEHA or the Labor Code. The United States Supreme Court has expressly stated that the FAA requires no such thing: the FAA makes arbitration agreements "as enforceable as other contracts, *but not more so*." (*Prima Paint Corp. v. Flood & Conklin Mfg. Co.* (1967) 388 U.S. 395,404 n.12) (emphasis added).

AB 51 explicitly states that it does not preempt the FAA

AB 51 added Section 432.6 to the Labor Code. Subsection (f) explicitly states: "Nothing in this section is intended to invalidate a written arbitration agreement that is otherwise enforceable under the Federal Arbitration Act." (Lab. Code, § 432.6, subd. (f).)

Conclusion

The template brief above was drafted to educate plaintiffs' employment lawyers about AB 51. To see how these arguments are being played out in current litigation, below are examples of arguments made by those defending AB 51 before the Eastern District of California:

"Because AB 51 applies to all forms of alternative dispute resolution…it does not discriminate against arbitration." (*Chamber of Commerce of the United States et al. v. Becerra et al.*, No. 2:19-cv-02456 (E.D. Cal.), Defendants' Opposition to Motion for Temporary Restraining Order, filed Dec. 20, 2019, ECF No. 14 at 6.) "AB 51 will prohibit only unilateral, employer-imposed arbitration provisions; it does not prevent parties from entering into arbitration agreements voluntarily." (*Ibid.)*

AB 51 is consistent with the FAA principle that arbitration "is a matter of consent, not coercion." (*Id*. at 1 (quoting *Stolt-Nielson S.A. v. AnimalFeeds Int'l Corp*. 559 U.S. 662, 681 (2010).)

While AB 51 did not take effect on January 1, 2020, SB 707 did take effect that day and now consumers and employees have remedies when companies strategically withhold payment of arbitration fees in order to stall or impede arbitration proceedings.

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