What Calif.'s New Arbitration Law Means For Employers

By **Emma Husseman and Thomas Kaufman** (November 13, 2023)

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On Oct. 10, California Gov. Gavin Newsom signed into law S.B. 365,[1] a bill that amends California Code of Civil Procedure, Section 1294.[2]

The new law provides that when a party appeals an order denying a motion to compel arbitration — an order that is immediately appealable — the trial court is not obligated to stay the action during the pendency of the appeal.

The law marks a major shift in California civil procedure law. Under the previous version of California Code of Civil Procedure, Section 916,[3] trial courts were generally required to stay proceedings while a denial of a motion to compel arbitration is appealed.

S.B. 365 will now force employers to litigate the underlying claims while pursuing such an appeal unless the trial or appellate court can be persuaded to exercise its discretion to order a stay.

Proponents of the bill argue that the proliferation of arbitration agreements, specifically employment arbitration agreements, have led to unnecessary motions to compel arbitration that delay determining employees' claims on the merits.

California Sen. Scott Wiener, who introduced the bill, claims that frivolous motions to compel arbitration by companies have delayed justice for consumers and workers.[4]

On the other hand, critics of the bill note that removing the protection of an automatic stay of trial court proceedings undermines the key purpose of arbitration: efficient, cost-effective litigation of claims.

Additionally, there is a risk that parties may feel forced to settle to avoid the threat — and expense — of concurrent trial court and appellate proceedings.

Coinbase Decision

The Federal Arbitration Act often preempts state laws that restrict the right to arbitrate. It is unclear whether the FAA will be held to preempt S.B. 365.

However, in a recent decision from this term, Coinbase Inc. v. Bielski,[5] the U.S. Supreme Court resolved a circuit split over whether the FAA requires district courts to stay proceedings during the interlocutory appeal of a denied motion to compel arbitration.

The Supreme Court held that such a stay was mandatory even though there is no express command in the text of the FAA for such a stay.[6]

In this decision, the Supreme Court held that, while there is no provision in the FAA directly addressing whether an action must be stayed during the pendency of an appeal of an order refusing to compel arbitration, such a rule was implicit in the structure of the FAA.

The Supreme Court recognized the background principle that an appeal generally divests a

district court of its jurisdiction over any aspect of a case involved in the appeal.

Furthermore, a key policy goal of the FAA is to promote the basic benefits of arbitration, such as efficiency, lessened expenses and less intrusive discovery.

If a party lacked the ability to stay a trial court action while seeking to appeal a denial of arbitration, but the court of appeal ultimately agreed the matter was arbitrable, that would undercut the value of arbitration in that the parties would be required to expend substantial resources litigating in court where that should not have been required.

Accordingly, under the highest authority interpreting the law, the FAA provides for automatic stays of an appeal.

The question is whether that policy standing alone is deemed important enough to preempt state laws to the contrary.

That is, California is not challenging the right to immediately appeal a denial of arbitration, and it is also not eliminating the possibility of obtaining a stay at the discretion of the trial or appellate court.

It is, however, undermining the potency of the right to immediate appeal.

Proponents of arbitration will certainly argue that states are preempted from taking any steps to dilute the ability to appeal without incurring the full cost of litigating in the trial court.

Regardless of the FAA's express provisions, given the Supreme Court's emphasis in Coinbase on the act's key policy goal to promote the basic benefits of arbitration, S.B. 365 may be preempted.

It remains to be seen how courts will decide this argument.

Takeaways

S.B. 365 will take effect Jan. 1, 2024, so employers should be aware moving forward that, assuming the law takes effect, they will need to persuade the trial court to stay an action during the pendency of appeal rather than having the right to obtain such a stay in all cases.

Additionally, employers need to be aware of potential increased costs if it becomes necessary to defend against continuing trial court proceedings and an appeal of the denial of a motion to compel arbitration. These increased costs should be considered in the settlement decision-making process as well.

S.B. 365 does away with an automatic stay of trial court proceedings. However, trial court judges will still be able to stay proceedings on a discretionary basis.

Given the concerns of proponents of arbitration surrounding the efficiency of arbitration and waste of judicial resources, many trial courts may still be inclined to stay proceedings.

Employers should be prepared to argue why and how continuing trial court proceedings would affect the efficiency of litigating the matter and the potential waste of resources to convince the trial court judge to stay the proceeding.

As S.B. 365 takes effect and we begin to see whether state court judges will continue to

stay proceedings on a discretionary basis, researching the assigned state court judge's attitude toward arbitration will be an even more important step in deciding whether to seek a peremptory challenge of the judge.

S.B. 365 makes peremptory challenges even more important to avoid concurrent litigation of an appeal of a denial of an arbitration motion and the underlying trial court proceeding.

S.B. 365 also heightens the importance of removing cases to federal court where possible, as district courts are likely more willing to enforce FAA principles than state courts.

Employers should ensure that any arbitration agreement expressly states that it is governed by the FAA. If S.B. 365 is preempted by the FAA, this will allow employers to avoid the California Arbitration Act subject to S.B. 365.

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[1] California Senate Bill 365, 2023, https://legiscan.com/CA/text/SB365/id/2845276/California-2023-SB365-Chaptered.html.

[2] California Code of Civil Procedure Section 1294, https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=CCP§ionNum=1294.

[3] California Code of Civil Procedure Section 916, https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=CCP§ionNum=916.

[4] See Senator Wiener Introduces Legislation To Stop Corporate Arbitration Abuse, February 10, 2023, https://sd11.senate.ca.gov/news/20230210-senator-wiener-introduces-legislation-stop-corporate-arbitration-abuse#:~:text=The%20bill%20establishes%20that%20an%20appeal%20of%20a,Association%20%28CELA%29%20and%20Consumer%20Attorneys%20of%20California%20%28CAOC%29.

[5] Coinbase, Inc. v. Bielski, 143 S. Ct. 1915, https://www.supremecourt.gov/opinions/22pdf/22-105_5536.pdf.

[6] See Supreme Court Eases the Ability for Employers to Appeal Denials of Motions to Compel Arbitration in Federal Court. https://www.laboremploymentlawblog.com/2023/07/articles/scotus/supreme-court-eases-the-ability-for-employers-to-appeal-denials-of-motions-to-compel-arbitration-in-federal-court/.