Kentucky Supreme Court Invalidates Employer's Arbitration Agreements

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Background

When there is a conflict between a federal law and a state law, the Supremacy Clause in Article 6 of the U.S. Constitution usually dictates that federal law trumps the state law. For example, the Federal Arbitration Act (FAA), which encourages arbitration as a potentially less costly, less formal means of resolving claims, overrides state laws which impede arbitration. Indeed, the U.S. Supreme Court has decided that any state law that discriminates on its face against arbitration is preempted by the FAA. Kentucky employers are familiar with this issue from last year's Kindred Nursing Centers decision, which FBT wrote a client advisory about at the time. In that case, the U.S. Supreme Court determined that a Kentucky law requiring an agreement to contain a "clear statement" waiving a right to a jury trial violated the FAA, because it treated arbitration agreements less favorably than other agreements. That case, decided by a 7-1 vote, sent a clear message that the FAA would preempt any state law that resulted in the negative treatment of arbitration agreements.

Decision

In a typical employment dispute between the Northern Kentucky Area Development District (NKADD) and a former employee who had signed an arbitration agreement as a condition of employment, NKADD moved to compel arbitration based on the arbitration agreement. The employee argued that it was void because of a Kentucky statute, KRS 336.700(2), that prohibits compulsory arbitration agreements as a condition of employment.

The statute states that "no employer shall require as a condition or precondition of employment that any employee or person seeking employment waive, arbitrate, or otherwise diminish any existing or future claim, right, or benefit to which the employee or person seeking employment would otherwise be entitled." Employers knew of this statute but implemented arbitration agreements based on U.S. Supreme Court and FAA edicts requiring FAA preemption.

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Federal courts and state trial courts have previously deemed KRS 336.700(2) to be preempted and therefore invalid. The Kentucky Supreme Court recently disagreed.

The language of KRS 336.700(2) clearly disfavors arbitration agreements on its face, explicitly stating that employers could not require employees to sign arbitration agreements as a condition of their employment. Despite this, the Kentucky Supreme Court leaned on the fact that the statute does not prohibit voluntary arbitration agreements to find that KRS 336.700(2) does not "actually attack, single out, or specifically discriminate against arbitration agreements." The court focused on the circumstances in which arbitration agreements are voided, rather than the fact that they are voided at all. Notably, the Kentucky Supreme Court's reasoning is not supported by any applicable employer-employee relations legal framework, nor has its reasoning been adopted elsewhere.

The Bottom Line

This ruling has the possibility of effectively invalidating all arbitration agreements that Kentucky employees were required to sign as a condition of their employment; however, the issue may not be over. NKADD has the right to request re-consideration, which is rarely granted, or it may seek review by the U.S. Supreme Court, which is even more rarely accepted. Employer groups will also be requesting that the General Assembly exercise its power to repeal KRS 336.700(2). Meanwhile, an issue resolved for employers in other states may be debated by Kentucky lawyers for years to come.

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