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PRESTON v FERRER

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Preston v Ferrer/The Federal Arbitration Act takes precedence over any state legislation granting exclusive jurisdiction to the state courts or another adjudicatory body to determine a dispute governed by an arbitration clause. Accordingly, the arbitration clause will trump the exclusive jurisdiction clause.

US Supreme Court, 128 S. Ct. 978 (2008)

Introduction

By this decision, the US Supreme Court adds to its line of authority confirming the sanctity of arbitration agreements, rejecting in this case the intervention of an administrative authority under California State law.

Facts

The factual background of *Preston v Ferrer* is simple. Mr Ferrer appears on a US television show as "Judge Alex". Mr Preston is an attorney practising within the entertainment industry who provided some services to Mr Ferrer. Under the terms of an agreement between them, arbitration is required of "any dispute [...] relating to the [contract's] terms [...] or the breach, validity, or legality thereof [...] in accordance with [American Arbitration Association ("AAA")] rules."

In June 2005, Mr Preston commenced arbitration, claiming some fees that he alleged were due to him from Mr Ferrer. Mr Ferrer claimed that Mr Preston had acted as an unlicensed talent agent in violation of California's Talent Agencies Act (TAA). Mr Preston contended that he had acted as a personal manager not governed by the statute. If it could be proved that Mr Preston had acted in violation of the TAA, the agreement between the parties would have been unenforceable and Mr Preston would not have been able to claim the fees he said were due from Mr Ferrer.

Mr Ferrer then petitioned the California Labor Commissioner for a determination that the contract was invalid and unenforceable under a provision of California state law contained in the TAA, claiming that Mr Preston had acted as a talent agent without the required licence.

Earlier proceedings

The parties brought the question of where the dispute should be decided before the courts. Mr Ferrer filed a suit seeking to enjoin arbitration. Mr Preston asked the court to compel arbitration. At first instance, the Los Angeles Superior Court denied Mr Preston's motion to compel arbitration and enjoined him from proceeding with the arbitration until the Labor Commissioner decided that she did not have jurisdiction over the case. Mr Preston appealed.

The California Court of Appeal upheld the lower court's judgment. It considered that the TAA gave the Labor Commissioner exclusive jurisdiction over the dispute. While the appeal was pending, the case of *Buckeye Check Cashing, Inc v Cardegna* 546 US 440¹, was decided by the Supreme Court. In *Buckeye* the plaintiffs claimed that the contracts at issue were illegal under state law and were thus void *ab initio*. The Supreme Court held in that case that challenges to the validity of a contract requiring arbitration of a dispute should ordinarily "*be considered by an arbitrator, not a court*". The California Court of Appeal distinguished the facts in Preston from those in *Buckeye* on the basis that it did not involve an administrative agency with exclusive jurisdiction over the dispute. The California Supreme Court denied Mr Preston's petition for a review of the California Court of Appeal's judgment. However, the US Supreme Court agreed to consider the issue of whether a state law giving initial adjudicatory authority to an administrative agency—in this case the California TAA—is overridden by federal law.

The Supreme Court

The case came before the Supreme Court on a writ of *certiorari*. Mr Ferrer argued that *Buckeye* should be distinguished on the basis that the TAA merely requires exhaustion of available administrative remedies before arbitration takes place. He submitted that the TAA was compatible with the Federal Arbitration Act (FAA) because the provision of the TAA giving the California Labor Commissioner exclusive jurisdiction to determine whether Mr Preston had acted as an unlicensed talent agent merely postpones arbitration of the dispute. Mr Ferrer asserted this argument for the first time before the Supreme Court. However, the argument did not sit easily with the fact that Mr Ferrer was also seeking a finding from the California Labor Commissioner that the whole contract was invalid. Had Mr Ferrer been successful before the Labor Commissioner, he would no doubt have argued that her ruling precluded an arbitrator from making any finding to the contrary. Indeed, the role of the Labor Commissioner in such circumstances would have been that of an independent arbiter of one of the issues in the dispute—that would have been precisely the role which the parties had agreed to reserve to an arbitrator when they entered into their agreement.

The Supreme Court reversed the California Court of Appeal judgment, finding by a majority of eight justices to one (Thomas J. dissenting) that when parties agree to arbitrate all disputes arising under a contract, the FAA trumps a state law that awards jurisdiction to some alternative forum. An important point to bear in mind is that this simply determines who decides whether Mr Preston acted as an unlicensed talent agent in violation of California State law; it does not affect whether or not the substantive law applies.

This was a case of a straightforward conflict between the state law (the TAA) and federal law (the FAA). The TAA grants the California Labor Commissioner exclusive jurisdiction over an issue the parties agreed between themselves to arbitrate. Proceeding as Mr Ferrer suggests, by delaying arbitration until the Labor Commissioner has made her decision, would be contrary to the intention of the lawmakers that parties should be moved into arbitration quickly and easily (*Moses H. Cone Memorial Hospital v Mercury Constr. Corp* 460 US 1).

The Supreme Court found that the best way to harmonise the apparently conflicting state and federal rules was to consider that California law relating to the substantive rights and obligations of the parties would apply, but the particular rules relating to the authority of the arbitrators would not.

Comment

The FAA declares a national policy favouring arbitration where parties agree to use that method of resolving disputes between them. Numerous cases have confirmed that this principle applies, despite repeated attempts to

¹See *Buckeye Check Cashing, Inc v Cardegna*, casenote by Jane Wessel and Alyssa Gsell [2006] Int. A.L.R. N-14.

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undermine the enforceability of arbitration agreements. A vexed question has been who decides whether an agreement to arbitrate or a contract containing such an agreement is valid. The firm answer arising from the Supreme Court is that it should be the arbitrator or arbitration panel who decides. The Supreme Court has held that questions concerning a contract's validity are within the arbitrator's jurisdiction, in cases grounded in federal law (*Prima Paint Corp v Flood & Conklin Mfg. Co* 388 US 395), state law (*Buckeye*) and now also where an administrative rather than judicial authority is alleged to have jurisdiction to determine the issue.