

# Searching out new ways through the crisis

The increase in company disputes arising out of the declining economic situation across Iberia is placing further strains on Spain and Portugal's domestic courts, say lawyers, and as a result now is the time to increase the potential benefits of other forms of dispute resolution, notably arbitration.

**A**cross Iberia, lawyers report an upturn in disputes which they say is being driven by the declining economic situation. Research by Iberian Lawyer highlights the collapse of the capital markets and of company valuations is prompting businesses to revisit agreements, an increase in debtor and creditor disputes, company restructurings and associated labour disputes, and inevitably prompting a rise in contentious issues emanating from the growing number of company insolvencies.

A key issue that parties in dispute face however is the limited ability of the national courts to cope with such a further upturn in litigation, say lawyers. Most are already over-stretched and under-staffed, and lack the resources, technology and financial support to improve either their processes or efficiency.

The hope of many practitioners is therefore that more appropriate dispute resolution mechanisms (ADR), notably arbitration, may begin to come into their own. The relative speed and efficiency of the processes offers parties a clear advantage, when compared to the domestic courts. But issues remain in convincing clients to use the process, admit many. Domestic Iberian clients continue to perceive arbitration as a risk while concern continues over a perceived lack of capable and qualified arbitrators, and arbitral institutions.

## Prevailing situation

"In 2008 there was a significant increase of litigation cases related to insolvency and unfortunately there is no reason to believe that this trend will alter during 2009. The fact that

real estate companies have been driving the Spanish economy for years but have simultaneously become one of the main casualties of the economic crisis offers a gloomy perspective from a litigation angle," says Vicente Sierra, head of litigation and arbitration for Freshfields Bruckhaus Deringer in Spain.



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An inevitable consequence of the economic collapse, say lawyers, has been a dramatic rise in disputes from the real estate and construction sector, and of course now a rising number of issues emanating from company insolvencies.

"An important number of clients from different sectors, but mainly construction and real estate, are seeking legal advice in debt restructuring, pre-insolvency and early termination of projects," say Francisco Peña of Gómez-Acebo & Pombo, which is currently advising Martinsa-Fadesa through Spain's largest ever bankruptcy.

A downturn in sales and company values is also prompting demand for advice on renegotiating or abandoning previously agreed deals, including exiting joint ventures, contractual breaches and securities litigation – with lawyers reporting the increasing integration of corporate and litigation teams to cope with the demand for specialist expertise.

Labour departments too are seeing an inevitable increase in demand as companies' restructuring processes impact on their workforces. "Insolvencies and enforcement of securities will likely be the main disputes that our clients will face over the coming months, while collective redundancy processes and claims based on breach of contracts and damages will affect many companies also," says Antonio Vázquez-Guillén, partner at Allen & Overy – which has doubled its litigation capacity in recent months.

Others in Portugal as well as Spain see growing stresses between businesses, their supply chains and customers.

"Clients should be prepared for default of payment in general terms from their customers. We also believe that many will be facing increased concerns in their relationships with banks and financial entities," says Nuno Líbano Monteiro, head of litigation at PLMJ.

Félix Montero at Pérez-Llorca in Madrid agrees, and notes an increasing emphasis by banks on ensuring that their finance agreements stand up to scrutiny in the event of a company insolvency. "Debtors need therefore to be prepared to fully negotiate with creditors – to pre-empt any issues before the banks decide that a situation is already lost. The finance arena has changed completely."

The result many lawyers believe is that the current levels of disputes will inevitably further increase.

El incremento de los conflictos en la empresa como consecuencia de la decadente situación económica en la Península Ibérica está poniendo más presión en los tribunales de España y Portugal, según comentan los abogados, los cuales están sobrecargados de trabajo y faltos de personal. A consecuencia de esto ahora es el momento de demostrar a los clientes, las ventajas de otros métodos de resolución de conflictos, como el arbitraje, un proceso sobre el que muchas empresas todavía tienen una visión equivocada.



"This year will be one of economic and social crisis. Labour unrest and insolvency disputes will increase significantly. Clients will be more cost conscious and will pay for legal strategies to reduce their costs and optimise debt recovery," says José Alves Pereira of Alves Pereira & Teixeira de Sousa in Lisbon.

### The judicial process

A key issue for Spain and Portugal's courts is therefore their ability to cope with the growing contentious fall-out from the prevailing economic crisis, say lawyers.

"Spain's commercial judges are having a difficult time. They are very well trained and talented but are few in number, lack sufficient resources and the excessive workload is affecting their ability to cope with increasing litigation," says Josep Maria Julià at DLA Piper in Madrid.

Spain's dedicated Mercantile Courts (*Juzgados de lo Mercantil*), are considered to have been a success but as they have exclusive jurisdiction over insolvency matters most are now near to collapse as a result of the sheer volume of work they are now facing. "We do not need any more legislative amendments, what we need is more infrastructure and more resources," agree Marius Miro Gili and Jordi Calvo Costa of Roca Junyent.

The situation is the same in Portugal, say lawyers there. "Portuguese domestic courts, especially the Lisbon Civil Court, are not prepared to face the accrued litigation expected. A special mention should also be made of Lisbon's Commercial Court, which handles insolvency proceedings but is already undermanned, with only four judges serving, and which with a transfer to a new location will certainly upset the already slow pace," says Líbano Monteiro at PLMJ.

A combination of overwork and understaffing is therefore creating a vicious cycle of backlogs and discontent across Iberia, say lawyers, made worse by questionable paperwork practices, and, in Spain recently, strikes, stoppages, and the defection of judges to private practice.

"The Spanish courts need personnel and money, and lots of both. The exodus of capable judges and the recent judicial strikes bode ill for the future, and not much money is likely to be forthcoming. So long as the courts are overworked and understaffed, their efficiency and attraction will be severely limited," says Cliff Hendel, at Araoz & Rueda in Madrid.

Portugal's courts have though already benefited from the implementation of procedures intended to simplify and speed up the judicial process, but this takes time to produce results, says Frederico Gonçalves Pereira at Viera de Almeida. New "order for payment" procedures intended to allow faster credit recovery have been introduced, but the courts still face difficulties associated with a lack of staff and internal bureaucracy says Ana Cláudia Rangel at Raposo Bernardo in Lisbon.

"Lisbon's Commercial Court is a good example of this situation. Even after the new processes were published, in order to simplify the Insolvency procedure, it is facing several problems since they have thousands of Insolvency proceedings to which they can't respond promptly."

### Exploring alternatives

Despite recent announcements that Spain is now likely to see a further expansion of the Commercial Court system the continuing lack of efficiency has prompted many lawyers to suggest that it is now up to them to suggest and provide credible alternatives for clients.

"Litigators must inform their clients that in most cases the average term to have an enforceable Judgment is 18 months. Alternative disputes resolution methods should be recommended to clients – unfortunately however there is not a culture of mediation in Spain, mainly because it needs a civil procedure law reform that has not been initiated," says Fernando González of Hammonds in Madrid.

The hope of many practitioners is therefore that it will be Iberia's arbitration institutions that respond, the discontent of clients with the court system providing an opportunity to demonstrate the relative speed and efficiency of the process.

Arbitration is much more popular than mediation, which is still incipient in the commercial world," says António Andrade de Matos at Rui Pena Arnaut.

Arbitration more efficiently provides the services clients need to expedite the dispute resolution process, agrees Ramon Mullerat of KPMG. "Parties can choose efficient time-conscious arbitral institutions and arbitrators who are independent and competent."

### Raising awareness

But despite the belief by practitioners of the inherent advantages of arbitration over litigation – its speed, efficiency and ability of parties to constitute an arbitration panel with specialist expertise – lawyers nonetheless continue to see reluctance particularly among domestic clients to choose the process, even in the face of the worsening domestic court situation.

The increasing confidence of Spain's international companies to adopt arbitration is in part due to the success of the Club Español del Arbitraje (CEA), which under the Presidency of Garrigues' managing partner, José Maria Alonso, members say, has helped encourage big law firms to support arbitration and this has inevitably also helped raised its profile among their major clients.

"Raising awareness of the benefits of arbitration and encouraging an increase in the number of arbitrators is one of the key goals of the Club. At the same time, important initiatives are being taken to widen the base of arbitrators, as in the case of the Court of Arbitration of the Madrid Bar Association, which has received over 700 applications from lawyers interested in acting as arbitrators," says Alonso.

In contrast to the international context, where many clients see arbitration not so much as an alternative but the only feasible way to reach a final decision on a dispute, cultural misconceptions continue to limit the domestic appeal of arbitration, say many.

"There have been major domestic arbitrations but some businesses have also been disappointed. The main issue is that the party appointed arbitrators are often simply the watchdog of the side that appointed them and the Chairmen sometimes struggle as they are not experienced enough," says Bernardo Cremades, founding partner of Cremades & Asociados.

Some parties, he suggests, now insist on having



a non-Spanish arbitrator. It is a position that helps explain the rising profile of the relatively small number of qualified and capable foreign lawyers practising in the arbitration arena in Spain. Among them are lawyers Cliff Hendel at Araoz & Rueda and Calvin Hamilton at new firm Hamilton, Swiss lawyer Jean-Marie Vellumin Froriep Ringgli, and Cremades' fellow partner, New Zealand-born, David Cairns.

Hendel, who was previously with White & case in Paris, reports that the past year has seen his arbitration practice increase from less than 25% last year to more than 75%.

But there remains the perception that there is lack of autonomy among arbitrators, says Hamilton. "If we begin from the premise that parties, rather than pick an arbitrator based on their qualifications, do so based on an effort to stack the tribunal, and sometimes do succeed, the outcome is often a miscarriage of justice."

The arbitration community is not however sitting idle in the face of such criticism. The matter of arbitrator independence has recently been highlighted by a Code of Best Practice drawn up by the CEA.

"The codes of best practices promoted by professional circles, and, in particular, the CEA, endorse a strict application of the independence rule. The IBA guidelines on conflict of interests are gaining acceptance as a general rule and arbitrators more often disclose relevant facts and circumstances according to such guidelines," adds Miguel Virgós of Uría Menéndez in Madrid.

### Transparency

A related issue, suggest some, is the need also to modernise Iberia's arbitral institutions. The preference of some to maintain a "closed" list of recommended arbitrators adds a further barrier to attracting the best candidates as arbitrators, as well as bringing the potential for extra costs and delays.

"An elitist arbitration process means that it is still not sufficiently developed and easily accepted or accessible by a large percentage of the business community," says Manuel Barrocas, of Lisbon's Barrocas Sarmiento Neves.

In an effort to demystify its processes, the Tribunal Arbitral de Barcelona (TAB) has notably sought to publish its rules and to offer guidance on fees and its registered arbitrators. "We have now established a system where all the details of the arbitrators are accessible online as we think transparency is vital. Specialisation is also a bonus for arbitrators, the knowledge of the sector and industry is very important to be able to understand the conflict and provide a resolution," says Jesús de Alfonso Olivé, appointed President of the TAB in November 2008.

The "control" of procedures and proceedings by institutions is also an issue, say some. It is

more like the flawed domestic court system than a modern arbitration institution. As in a court case, communication between parties is administered through the arbitration institution. Delays can therefore be experienced by the smallest of issues, like arranging a time and place to convene.

"In international arbitrations the arbitrators and counsel effectively run the process, of course they copy in the arbitral institution on any correspondence but it is up to themselves, for example, to serve papers on parties. It was therefore a surprise to encounter the opposite system in some well-known arbitral institutions," says Cristian Conejero Roos, head of Latin American arbitration at Cuatrecasas, and formerly counsel for Latin America and the Iberian Peninsula in the International Chamber of Commerce (ICC).

Closed systems and lists, some suggest, encourages the perception of arbitration as an expensive "closed shop", although for some general counsel, the attraction of arbitration is not however in the relevant cost savings.

"Arbitration is now as expensive as litigation. At the end of the day, the only difference is time. Courts take up to 5 years and arbitration only 3 years," says one IBEX35 general counsel.

The shallow pool of experienced arbitrators available adds the potential for delay, but many believe that clients are willing to wait on the availability of the requisite arbitrators. "It is a common criticism that there are a closed group of arbitrators but if you want to find someone good and with the relevant experience then you will inevitably choose someone who is busy," says Bernardo Cremades.

Cremades is viewed by many as Spain's highest profile international arbitrator. From the independent Spanish experts Juan Fernández Arnesto and Miguel Angel Fernández-Ballesteros are also highly regarded. The incentive of a faster dispute resolution process is a major issue for the TAB, says Olivé. "The aim of the reconstituted new board of the Barcelona arbitration court is to increase users, in particular amongst medium and big businesses, with the objective to reduce the average resolution period from ten months to only six months."

### Number of institutions

Also confusing for users of arbitration is the proliferation of arbitral institutions, suggest some. We tend to think that Madrid is Spain and Spain is Madrid, without noticing the increasing use of arbitration across centres such as Valencia, Barcelona, Bilbao or Zaragoza, says one practitioner.

Lawyers cite however the reorganisation of the Corte de Arbitraje de Madrid (linked to the Madrid Chamber of Commerce) as an example of what can, and needs, to be achieved across Spain – it has adopted the CEA's proposed arbitration guidelines,

**2004**

Dr\*\*\*, Zurich, commenting on FR Madrid Office:

(ironic) *"What are you going to do in Spain?!"*

**2009**

The same:

(appreciative) *"What did you do in Spain!!"*

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in an attempt to win international as well as domestic users, including being able to operate in both Spanish and English.

"The CEA is trying to help lead the practice of arbitration in Spain and the drafting of a set of arbitration procedure rules for general use by arbitration forum goes some way in helping to do this. The Corte de Arbitraje de Madrid has already adopted the rules and we hope that others, such as the Corte de Arbitraje del ICAM (linked to the Madrid Bar Association) will also likely do so soon," says Antonio Hierro, head of arbitration at Cuatrecasas.

Many point to the success of this "Swiss Model", of unifying different arbitration institutions under common rules, as a potential way forward. Some even suggest that such an approach could even be extended to Latin American arbitral institutions, in order to help capitalise on Iberia's position as a conduit of European investment into the region.

The benefits of such an approach are not lost on Jean-Marie Vulliamin at the Madrid office of Swiss firm Froriep Ringgli. "It is an age of consolidation and of resisting the old customs, which for some Spanish arbitral institutions will mean having perhaps to leave aside some protectionist reflexes, abandoning the system of lists of arbitrators, accepting that institutions are not a centre of power, but a service to be rendered to the arbitral tribunals and the parties."

The situation in Portugal is however the reverse, suggest some lawyers, where most arbitrations continue to be concentrated through the Portuguese

Chamber of Commerce and Industry in Lisbon and the Associação Comercial do Porto.

"We strongly believe that the creation of regional arbitration centres would render them accessible and provide for the familiarisation with arbitration by the small and medium companies. This would not only promote arbitration but provide an inestimable help in reducing the flow of new judicial proceedings in the national courts," says João Paulo Teixeira de Matos of Garrigues in Lisbon.

### Outlook

The outlook for the Iberian economy may be poor, but for dispute resolution lawyers across Spain and Portugal the opposite is clearly true. The counter-cyclical nature of a law firm may be a cliché but in the current economic situation it seems true. Firms with strong litigation and arbitration practices report that they are tremendously busy with no sign of a slowdown in demand over the coming year.

The challenge such an upturn presents however is expectation management. Neither Spain nor Portugal are countries in which it is possible to reach any kind of judicial satisfaction in a hurry.

As a result, lawyers suggest that clients increasingly need to consider dispute resolution strategies as part of their standard contractual processes, the relative benefits of adopting litigation and arbitration clauses, and perhaps of adopting less adversarial means of solving disputes.

Reforming the judicial system entails definitely institutionalising the paradigm of turning to courts only as the last resort and reinforcing alternative means of dispute resolution, says Jorge de Abreu at Abreu & Marques e Associados in Lisbon. "These alternative means must be seen as a solution of quality rather than quantity," agrees fellow partner Filipe Lobo d' Avila.


Lawyers acknowledge though that alternative dispute resolution remains in its infancy across Iberia. "It is still not the case that arbitration clauses are agreed in clients' daily commercial relationships, although they are well understood for more sophisticated transactions, which though will be hardly affected by the current economic situation," says Raúl da Veiga at Gómez Olmo & Da Veiga (Gold) Abogados.

But despite the continuing challenges faced most lawyers remain optimistic as to the future of arbitration within Spain and Portugal, and ultimately their position in the international arena.

"In Portugal the judges are very supportive of arbitration, but it remains necessary to work closely with lawyers to explain the advantages of using arbitration. There are cases that are appropriate and others that might not be," says Rui Botica Santos at Coelho Ribiero & Associados.

For the time being, arbitration remains however the choice of a domestic minority and further effort will continue to be required to overcome still prominent cultural barriers and misconceptions.

"The Spanish courts have proven co-operative with international arbitration, a new generation of arbitrators with extensive international experience is at work and Spanish institutions are openly supporting arbitration. It is therefore only a question of time before all these elements come together and arbitration becomes a more popular alternative at home," says Manuel García-Villarubia at Uría Menéndez.



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