## Dispute Resolution Report 2012: Hanging up the gloves

**In a downturn it is law firms' litigators and arbitrators that become the stars, goes conventional thinking. A drop in transactional activity may be matched, or even exceeded, by a rise in disputes. There has been a huge rise in the number of cases but this is also bringing a need for new approaches to resolving them, meaning lawyers must have more weapons in their armoury. Companies must be prepared to fight, but they must also be open to talk.**

"There has been a clear upturn in litigation and arbitration since the onset of the financial crisis and in many cases these disputes are much more complex than before," says Mercedes Fernández, Managing Partner of Jones Day in Madrid.

Cases are rising further up the corporate agenda, with shareholder, contractual and finance disputes more common. The way businesses approach such claims is therefore taking more strategic importance. Three years into the downturn and lawyers question whether they are riding a still-growing wave of claims.

"The financial crisis is far from over and we believe that we are nowhere near a peak in the number or type of disputes being seen," says Carlos de los Santos Lago, disputes Partner at Garrigues. "However, the number and relevance of judicial disputes has not been as significant as one would have expected when the crisis first broke."

Lawyers may debate whether firms' litigation and arbitration practice are truly anti-cyclical but nonetheless agree that in the past few years they have become busier than ever as the economy has turned bad. "I am not sure if litigation is a real counterbalance but it has certainly grown in weight relative to the levels of corporate activity seen at our firm," says Miguel Virgós, Partner at Uría Menéndez in Madrid.

### A rising trend

Since the onset of the financial crisis in 2007, and the bursting of Spain's real estate bubble in 2008, the downturn has seen a rise in specific kinds of disputes. With a dramatic increase in claims arising out of the construction and financial sectors – including mis-selling claims – and an inevitable spike in insolvency and bankruptcy-related actions.

"In my opinion, the economic crisis has generated a new type of judicial procedure on the basis of bank or financial contracts of complex figures, financial derivatives and swaps, and in regard to which I don't believe that we are anywhere near reaching the maximum peak," says Jordi Calvo, litigation Partner at Roca Junyent.

Likewise, lawyers report that the hangover from the transactional boom of the last decade is also now being played out in the courts. "We have seen a large number of claims emanating out of corporate transactions entered into before the downturn, which have turned out not to have met the parties' expectations in one way or another," adds Fernández at Jones Day.

According to some sources, insolvencies in Spain have increased by nearly 20 percent over the last year alone, further overwhelming the Commercial Courts.

"Construction companies and real estate developers continue to lead the number of insolvency requests. Unfortunately, in 2012 we will continue to see intense activity by the Commercial Courts in relation to such proceedings," says Guillermina Ester, litigation and arbitration Partner at Pérez-Llorca. "Additionally, banks are continuing their recovery proceedings, mainly related to the enforcement of mortgage loans."

**Regulated sectors**

In Portugal, the same trends are clearly evident, say lawyers. Financial pressures are bearing down on companies and more are wrestling with their contractual obligations. In addition, the downturn has been characterised by an upturn in claims between regulated businesses.

"There is a rise in issues across all areas of the economy, but we have seen peaks in specific sectors, notably banking, telecoms and in industrial sectors, where companies are short of liquidity but the competition is most fierce," says Frederico Goncalves Pereira, Head of Disputes at Vieira de Almeida (VdA) in Lisbon.

Here too there is a perception that we have not yet reached the crest of the wave in the number nor value of claims, especially in areas such as commercial litigation and debt recovery.

"Companies have experienced a large increase in the number of cases involving real estate guarantees such as liens and mortgages, while the number of insolvency cases has grown exponentially," says Nuno Líbano Monteiro, Head of Insolvency & Restructuring and Litigation at PLMJ. "But 2012 will be

economically and financially far more complicated and this means that litigation will increase; we will see a significant further rise in the number of non-performing loans, foreclosures and in insolvency proceedings."

The downturn is therefore all-pervasive and businesses have to adapt their operations and strategies according to reduced revenues. Among the most significant trends has been an increase in credit claims for very high amounts, debt recovery and proceedings by multinational companies led by commercial restructuring and insolvencies, as well as collective dismissals, says Sandra Ferreira Dias of Franco Caiado Guerreiro in Lisbon, among others.

It is no surprise that labour disputes continue to be on the rise. "There has been a significant increase in legal claims between employers and employees regarding the most sensible interpretation of labour rights including, for instance, even the concept of overtime," says Ana Claudia Rangel of Raposo Bernardo in Lisbon.

**Considered cases**

Yet despite the upturn in the volume of cases lawyers emphasise that formal disputes are not being entered into lightly. Cases are taking on greater strategic importance but companies are much more careful about costs of fighting them.

"We have seen a rise in contractual disagreements and disappointments, but clients are not filing claims without careful thought. They are much more conscious of the risks, the costs and the management time involved with pursuing claims," says José María Alonso, Head of Dispute Resolution at Baker & McKenzie in Madrid, and member of the Steering Committee of the Global Arbitration Group.

Both the merits and demerits of pursuing a case are being more carefully analysed, many emphasise. "As a consequence of the downturn there has been a clear increase in debt recovery litigation however, with respect to complex commercial litigation we do not perceive a similar trend. Many clients are now increasingly hesitant to start cases due to the fact that they may result in significant expenses with an often uncertain outcome," says David Arias, Head of Litigation and Arbitration at Pérez-Llorca in Madrid.

An inevitable concern is the potential cost of making, and defending, a claim. With liquidity already tight, companies therefore increasingly want certainties over how much they are putting at risk.

Clients want their lawyers to be more creative in the ways in which they approach disputes, adds Arias. “There is also a clear move away from invoicing on an hourly rate basis and indeed for us, the application of fixed fees or other alternative fee arrangements is not a problem. There are always additional issues that come up in any case, but we are confident that we have the experience to foresee what may happen.”

The use of hourly rates in litigation is now therefore a thing of the past. “Clients want to manage their costs and part of this is driven by the fact that there is an increased number of disputes arising from cash shortage problems, which themselves are leading to very complex litigation cases,” says José Luis Huerta, Managing Partner of Hogan Lovells in Madrid.

The same drive towards certainty over costs and fixed fee arrangements is also evident in Portugal. “When there is money in the system conducting litigation is not perceived as a luxury, within a crisis environment it may be,” says Miguel Pinto Cardoso, Head of Disputes at Linklaters in Lisbon. Companies are therefore being most forthright when they believe they have the strongest of claims, suggest others. “It is not true that businesses are being flippant. Each claim comes with a cost, and in this environment everybody is more careful. Clients want to be cost effective and to ensure that they recover the money spent, and are looking more towards a combination of hourly rates with success fees,” agrees Fernando Aguilar de Carvalho, Disputes Partner at Uría Menéndez - Proença de Carvalho in Lisbon.

**Aggressive strategies**

For businesses that have the funds for litigation there is the question of the strategy to be employed. For some it may be a straight fight, but for a growing number of companies the launch of court proceedings is often a first step towards negotiating a settlement.

“It is difficult to make a statement that is valid in general terms, but we do now see people go to trial for things that some years ago would have probably stayed out of court, simply because there has been a change of mentality. Companies and individuals have become both more nervous and aggressive,” says Francisco de Malaga, Head of Disputes at Linklaters in Madrid.

Some clients are though looking to find faster and more cost-effective solutions even if that implies having to waive some claims, say others. “It is an approach that presents a challenge for lawyers as it

compels us to constantly offer the proper advice to facilitate their negotiation objectives without undermining their legal position," says de los Santos Lago at Garrigues.

Others nonetheless believe that companies' evident willingness to resort to litigation is no different to that seen in previous times, it is just that there are significantly more claims. This has however two major effects, says Fernando Gonzalez of Squire Sanders in Madrid: "First, an increased frequency of out of court settlements, as many companies still prefer ultimately to avoid lengthy and costly litigation, and second, increased litigation concerning breaches of contract."

A more forthright position also works both ways. "Clients are more constructive in their use of litigation. However, the reverse is also true, given the downturn, the serious threat of litigation is also taken a bit more seriously by defendants," says Calvin Hamilton, Principal of Madrid boutique Hamilton Abogados.

More room for litigation means also that businesses are placing greater focus on avoiding disputes in the first place, note others.

"This is an important part of companies' overall negotiating strategy, as in the current economic scenario disputes are likely to arise sooner than expected. External counsel are increasingly being used as preventive instruments during negotiations, where their participation is perceived as an investment rather than a cost," says Gonzalo Stampa of Stampa Abogados in Madrid.

**Despite the evident pressures facing businesses, lawyers can still help clients to better focus their frustrations. "Parties become naturally less patient and flexible, although not necessarily more effective," says Antonio Teles, Partner at Sérvulo in Lisbon.**

Others in the market suggest that a rush to file a claim can anyway bring about unintended results. "In some cases, companies have used procedural means to force debtors to pay debts even if those procedures are manifestly inadequate: for instance, creditors have requested the insolvency declaration of their debtors merely to force them to pay," explains Miguel Esperança Pina Litigation Partner at Cuatrecasas Gonçalves Pereira in Lisbon.

Likewise adopting an aggressive litigation strategy can backfire. "I am not entirely convinced that choosing litigation is the best means of putting pressure on another party, unless each side has deep pockets and the best legal team," says Goncalves Pereira at VdA. "The only major instances in which we

see companies using litigation strategically is for private enforcement where no other alternative exists. But even here, in the telecoms or competition fields, it is only really the beginning of a trend."

In very complex cases, parties usually only ever resort to the courts when there is no other option on the table, say others. "Portuguese clients, relative perhaps to multinational businesses, are certainly less ready to enter into litigation," says Aguilar de Carvalho at Uría Menéndez - Proença de Carvalho.

**Alternative methods**

One tangible outcome of the upturn in cases has clearly been the overwhelming of many Commercial Courts, largely the result of a deluge of insolvency cases, say lawyers. Frustrations with the judicial process and delays in proceedings are however helping to push clients (some reluctantly) to consider other forms of dispute resolution methods. The primary alternative being arbitration, as both Spain and Portugal see the ongoing modernisation of rules.

Spanish companies still prefer to go to Court every time they consider that they are right, and often regard settlement as a sign of weakness, say lawyers, but the Arbitration Court of Madrid is reportedly now hearing its first billion euro claim.

"There has certainly been growth. But, as far as domestic arbitration is concerned, there still appears to be a degree of reluctance on the part of some Spanish companies. Some in-house lawyers do not want to go to their CEO and say that they have chosen domestic arbitration over litigation, they need to get more personally involved. After all, the client usually chooses the arbitrator but it never chooses the judge" says Arias at Pérez-Llorca.

The recurring issue is a lack of confidence in arbitration institutions and arbitrators, and unfamiliarity with the system, say others. "In general, companies accept that arbitration can provide a final solution to their disputes more quickly than the ordinary courts. Nevertheless, there are suspicions, particularly in relation to the impartiality and 'corporatism' of professional arbitrators," says Borja de Obeso, Partner with Gómez-Acebo & Pombo.

This perception is changing but very slowly, says Calvin Hamilton. It is a situation that is in direct contrast to the willingness of many international companies to choose arbitration almost by default. The most sophisticated clients are even now adopting a hybrid method to pursuing claims, he adds. "This involves

tiered clauses where the parties require that an attempt is made to reach an amicable solution, including a cooling-off period, prior to commencing litigation. Indeed, some Arbitration Tribunals are often being asked to decide whether or not the applicable cooling-off criteria has been met."

Lawyers in Portugal also agree that there is still an element of misunderstanding around the use of arbitration for domestic disputes, but concrete steps are being taken to reinforce parties' comfort in the system.

"We are seeing a rise in domestic cases as the Courts become increasingly overwhelmed and parties increasingly want to have someone who understands their business sector and the specific issues in dispute to decide their cases," says Cardoso at Linklaters in Lisbon. In Portugal, the construction sector is among the most advanced in the use of arbitration but more has to be done to ensure wider acceptance.

Resistance still exists as corporate and in-house lawyers are not familiar with ADR solutions and therefore contracts still do not usually contain specific clauses for it. "But the new UNCITRAL-inspired Portuguese Arbitration Law will hopefully help to speed the evolution," says José Miguel Júdice, Head of Arbitration at PLMJ.

The process is already obligatory in many IP disputes, while last December saw the approval of a new Voluntary Arbitration law, changing Portugal's Civil Code Procedure Act – recognising the enforcement of foreign arbitral awards, and the granting of interim injunctions.

"Clients seem to be willing to explore ADR methods, particularly arbitration. This has always been the case with international clients but there is a clear domestic trend as well, which has been further bolstered by the successful practice of commercial arbitration centres and the publication of a new and modern legal framework," says Tito Arantes, Head of Disputes at Uría Menéndez - Proença de Carvalho.

**Reforming the system**

The changes being seen by lawyers in the type and volume of case emerging out of the economic downturn therefore present new and different challenges, they say. Both in terms of their substance and the means by which they are increasingly being resolved.

In Portugal, the volume of cases and inefficiencies of the court system has finally moved the Government to propose significant reform to both the make-up and location of the Commercial Courts, including the creation of dedicated, IP, competition, regulatory and supervisory Courts. Moves are also underway to update the country's arbitration rules.

Such developments are broadly welcomed but some nonetheless suggest that the judicial system has seen prior change without success.

"There are procedural issues but mainly structural, like the effectiveness of court management to look after and schedule cases. Arguably we do not need major reform we just need more and better organisation," adds Miguel de Almada, Disputes Partner at Morais Leitão Galvão Teles Soares da Silva.

With a body of domestic expertise built up over decades and in challenging judicial and commercial environments, firms are also increasingly looking to export their disputes capabilities. It is an area of practice in which many Spanish and Portuguese lawyers believe they can complete with the largest international law firms.

"For disputes involving Portuguese or Spanish-speaking parties, I consider that there is no need whatsoever to look for expertise out of the Iberian arena," says Jose Alves Pereira, Partner with Alves Pereira & Teixiera de Sousa in Lisbon.

As Iberian businesses continue to grow internationally new opportunities are therefore opening up to lawyers. "In the old days the Spanish firms had much to learn from the global players in terms of conducting international cases, but nowadays we have done our homework, gained experience and provide the same level of services," says Arias at Pérez-Llorca.

Antonio Hierro at Cuatrecasas agrees. "For decades we have followed Spanish and Portuguese clients to Latin America and have built up a track record and experience of managing cases, alone and with local co-Counsel. It is hard to see how other international firms can be better placed to assist businesses across the region."

Despite the wave of claims now overwhelming the Courts and Tribunals lawyers acknowledge however, that situation is not one that is good for the economy or even their law firms.

Litigation and arbitration practices may be booming and teams working non-stop but clients' demand for more certainty over costs, a move towards fixed fee arrangements and a growing willingness to hang

up their gloves and settle more often, means that revenues may still not match the corporate groups in the boom years. Disputes lawyers may be riding to the rescue of their clients but they may not save the day for their law firms.

Source: Iberian Lawyer