

Estonia

Chamber of commerce:

Estonian Chamber of Commerce and Industry
Toom-Kooli 17
10130 Tallinn
Estonia
Tel: +372 6 04 00 60
Fax: +372 6 04 00 61
Email: koda@koda.ee
Web: www.koda.ee

Professional body:

Estonia Bar Association
Rävala pst 3
10143 Tallinn
Estonia
Tel: +372 6 62 06 65
Fax: +372 6 62 06 77
Web: www.advokatuur.ee

New developments in Estonian insolvency law

Vadim Filimonov
Paul Varul Attorneys-at-Law
Tallinn

Judicial corporate rehabilitation as an alternative to the liquidating bankruptcy procedure has been contemplated in Estonia since 2006. The need to limit the public cost of mitigating the present financial crisis has acted as a catalyst for the adoption, at the end of 2008, of a new Rehabilitation Act (*Saneerimiseadus*), which provides the means by which private parties can contribute to crisis resolution.

By April 28 2009, 48 petitions for corporate rehabilitation had been filed with the Estonian courts. At least 10 rehabilitation proceedings have been commenced.

Estonia has adopted a two-track approach: that is, bankruptcy and rehabilitation procedures are formally separated. The failure of a rehabilitation proceeding does not provide a ground for a simplified transition to bankruptcy. Estonian law does not allow for conversion from bankruptcy to rehabilitation. Within the bankruptcy procedure, special corporate recovery opportunities can be used.

Rehabilitation proceedings

The right to initiate rehabilitation proceedings is vested only with the debtor. The access to rehabilitation is quite easy, encouraging debtors to address their financial difficulties at an early stage. Prospective illiquidity is the most important criterion of the commencement of proceedings.

Estonian rehabilitation law is rather favourable to the debtor in the sense that it enables the debtor to retain full control over the operation of the business throughout the rehabilitation proceedings, thus creating an additional incentive to voluntarily make use of rehabilitation. However, debtors' activities are supervised by a court-appointed adviser,

who is nevertheless not in a position to block transactions made by the debtor.

Another immediate consequence of the commencement of a rehabilitation proceeding is a stay on the ability of creditors to enforce their legal remedies. The interests of creditors are safeguarded by prescribing a maximum period of 60 days from the date of commencement of the proceedings during which the rehabilitation plan should be submitted to the court.

It is the rehabilitation adviser who is given the exclusive opportunity to prepare the rehabilitation plan on the debtor's behalf. The plan will adequately disclose information regarding the financial condition of the company and propose measures for reorganisation of the company and the transformation of the legal rights of creditors. It is a general understanding that tax debts cannot be transformed by a rehabilitation plan. However, the commencement of rehabilitation proceedings seems to be a reasonable ground upon which to apply for payment of tax arrears in instalments. Among other measures for the transformation of creditors' rights, the law explicitly allows for debt-for-equity conversion without the consent of shareholders, which is a unique exception from the principles of Estonian company law.

Approval stages

There are two stages of the approval of a rehabilitation plan. The first is approval by a majority of creditors at a creditors' meeting or by remote voting. Given that the secured claims can also be transformed by the rehabilitation plan, the law allows for secured creditors to vote as a separate class. The division of unsecured creditors into different classes is also possible under the new Act. A hybrid test is used that requires a class approval by a majority in the total number of creditors in the class and by a two-thirds majority of the total debt of the class. There is no special provision to restrict the voting rights of insiders.

At the second stage of approval, the rehabilitation plan should be approved by the

court. Dissenting creditors can demand the rejection of the plan in, for example, a case of the unequal treatment of creditors. The court can also evaluate the feasibility of the plan and take other circumstances into account. There is also a mechanism that enables the court in some cases to approve the plan and make it binding on creditors, even if the plan has not been approved by the qualified majority of the total debt. The approval of pre-packaged rehabilitation plans (where the voting takes place before the commencement of the rehabilitation procedure) is disputable. Experience shows that, notwithstanding the rigid time limits, the court approval procedure may be protracted in Estonia, particularly if the initial court order is contested in higher courts and if some of the creditors are non-residents.

The rehabilitation plan can only be binding upon creditors to whom the plan and the notice calling the creditors' meeting have been handed over. The notion of handing over remains disputable in the new Act, and foreign creditors may need to notify their Estonian debtors of how they want to be informed of potential rehabilitation proceedings.

Although the ability to avoid pre-commencement transactions with insiders could be of considerable benefit to an enterprise that is using the rehabilitation procedure, the Estonian Rehabilitation Act does not contain such avoidance provisions.

Another problem with the Rehabilitation Act is that it does not provide for the adequate protection of post-commencement creditors. Given the importance of new financing for an enterprise during rehabilitation, it could be advisable to allow the rehabilitation adviser or the court to grant post-commencement creditors a special priority in the event of the debtor's bankruptcy. In fact, the post-petition creditor also bears the risk of the premature termination of the rehabilitation proceeding and the subsequent annulment of the rehabilitation plan, in which case the rights of other creditors are restored to the pre-commencement point.

If the rehabilitation plan breaks down or is found to be incapable of performance, the court may terminate the rehabilitation, with the result that the next rehabilitation proceeding can only be commenced in two years' time at the earliest.

It can be concluded that the new Estonian corporate rehabilitation law seems to be rather debtor-friendly, as the debtor has everything to gain and almost nothing to lose. The law could offer better protection to creditors by providing them with the opportunity to commence rehabilitation proceedings and propose rehabilitation plans by granting some priority to dissenting and post-commencement creditors, as well as by allowing for the avoidance of pre-commencement transfers and providing for power-sharing between the debtor and the rehabilitation adviser as regards post-commencement transactions.

Financial and corporate

Recommended firms	
Tier 1	Lepik & Luhaäär Lawin Raidla Lejins & Norcouis Tark & Co
Tier 2	Luiga Mody Hääl Borenius Sorainen
Tier 3	Eversheds Ots & Co Glikman & Partnerid Paul Varul Tamme & Otsmann

"It seems to me that Estonia is a bad word now," says one partner. Estonia, like the other Baltic countries, is struggling to attract international finance, meaning that law firms have to adapt to a new reality.

Restructuring and insolvency work is one practice area firms are looking to fill the gap left by falling revenues from banking, finance and M&A work. This is partly because the market demands it, but also because new legislation makes it possible to conduct restructurings similar to the US Chapter 11 procedure.

Banking and finance work is dominated by performing due diligence on loan securities and looking through lease agreements. No large new deals are on the horizon, and one partner says his corporate finance peers have told him: "You might as well go on sabbatical for the year."

The predicted avalanche of distressed transactions has yet to materialise, with

lawyers reporting that behind the scenes they are mandated to do due diligence by buyers looking at companies. Most of the deals disappear for any number of reasons, but price, finance and economic uncertainty are recurring explanations.

Finally, a touch of scandal hit the legal market when one key lawyer of an unranked firm faced charges of bribery. So far, the lawyer has been found guilty on first-instance charges.

Lepik & Luhaäär Lawin

Lepik & Luhaäär Lawin commands the market's respect, particularly in the banking and finance and M&A sectors. Clients like the firm's approach to its work: "They are different: they are more business oriented, more into M&A and have foreign clients," says one.

Martin Simovart is the firm's figurehead and is consistently highlighted as a leading lawyer. Partners note that his practice takes in most forms of financial and corporate work.

Simovart is backed up by some young talent. For banking and finance Ermo Kosk is seen as a young and aggressive partner who knows his way around a deal. On the M&A side one client notes that, "Gerli Kilusk is young and the most active; she is more on the ground".

In 2008 Kosk advised Pohjola Bank on its role as the borrower, security agent and lead arranger on Estonian financing and collateral issues in a loan facility. Lepik & Luhaäär also acted as lead legal advisor in the Baltic region on the deal.

Estonia's fluctuating currency has affected M&A deals, as one Kilusk is working on illustrates. She is representing Alta Capital Partners in its attempted purchase of dairy producer Tere and other various subsidiaries of Kalev. Negotiations continue, but the deal is expected to go through.

Kilusk also represented Bancroft Private Equity in a transaction that saw a consortium buy a majority stake in Starman, a cable and broadband operator. The purchase of shares was followed by a mandatory takeover and squeeze-out of minority shareholders, with the company then becoming a private enterprise.

Leading lawyers

Gerli Kilusk
Ermo Kosk
Martin Simovart

Raidla Lejins & Norcouis

Raidla Lejins & Norcouis is considered a powerhouse in the Estonian legal market. "They are the best without a doubt," says a competitor. However, it is felt that other firms have

narrowed the gap in recent years. The firm is strong in both banking and finance and in M&A work, but the market also notes it is establishing a presence in the burgeoning restructuring and insolvency practice area.

For banking and finance Raino Paron is consistently singled out as an expert, as is Sven Papp for M&A. In R&I the firm can turn to Martin Käerdi for expertise, as he worked on the new law relating to reorganisations.

Clients like the depth of service the firm can offer and the professional approach it brings. "The firm is able to cover any and all areas of law," says one client, who adds: "It is constructive in giving business-oriented advice and effective solutions."

Despite paralysis in the banking market, there is still financing available for the right project. Paron advised Tallink Grupp, a ferry operator, on securing a €132 million syndicated facility for the acquisition of a new ferry.

The firm worked on a pan-Baltic deal together with Roschier Raidla's offices in Latvia and Lithuania. The deal involved structuring the finance for acquisition of a real-estate portfolio in the Baltics worth €150 million. The firm represented Skandinaviska Enskilda Banken.

On the regulatory side, the firm has secured mandates advising Borse Dubai on Estonian law aspects of its proposed acquisition of the OMX and gave American law firm Davis Polk & Wardwell Estonian law advice regarding Visa's IPO.

Leading lawyer

Sven Papp
Raino Paron

Tark & Co

Tark & Co boasts strong names in both finance and M&A, with young but experienced partners Hannes Vallikivi and Risto Vahimets the driving forces behind the firm.

The firm has added four lawyers despite current trends in the legal market. Associate Kerstin Pilt is the most significant arrival, coming from the Estonian Financial Supervision Authority.

Vallikivi is the senior finance partner and worked on one of the few Estonia-originated transactions in 2009. The firm represented the city of Tallinn in the €31.4 million bond issue arranged by Nordea Bank. Representing the city again in November 2008, the firm advised on a €32 million project finance facility from the European Investment Bank.

In the same month the firm completed a €22.4 million financing for the shipping company Infortar Group. On the M&A side Vahimets has been busy too, advising the

buyer Ascar Tallinn in the 100% acquisition of Korea Auto.

The firm also advised Danske Bank on its cross-border merger with its Estonian subsidiary Sampo Bank in June 2008.

Leading lawyers

Hannes Vallikivi
Risto Vahimets

Luiga Mody Hääl Borenius

Commentators observe that Luiga Mody Hääl Borenius continues to grow and its presence on deals is becoming more and more noticeable. The firm possesses a decent stable of lawyers and has promoted three associates to partner level in the past year.

However, it is the more established partners that make the firm a force. Former managing partner Sten Luiga is noted as a wise head, while Priit Pahapill comes highly recommended for banking and finance matters. “Peeter Kutman is my favourite lawyer to have on the other side,” says one peer. “He is really skilled and is great with clients.”

The firm counts private equity house Baltcap as a regular client. One deal saw the firm advise on Baltcap’s purchase of Quattromed HTI Laborid. The firm also advised Baltcap on a pending agreement to purchase Ekspress Hotline from the Ekspress group.

Elsewhere, the firm counselled the European Bank for Reconstruction and Development (EBRD), a shareholder in Estonian Cell, on Estonian Cell’s restructuring of the shareholder process.

In an M&A deal the firm worked on the other side of the EBRD, advising Freenergy on the bank’s purchase of a 35% shareholding in the company for €18.9 million. The firm also advised Essilor International on the acquisition of shares in an Estonian optic company, Optika Hulgikaubanduse.

Leading lawyers

Peeter Kutman
Sten Luiga
Priit Pahapill

Sorainen

Sorainen is a young and ambitious firm that is pushing hard to catch up with the top-tier players. Rivals view it as an aggressive competitor, but clients like the way this approach is translated into service. “The service was tight, it was crunchy. They turned around the work quickly. It was relevant. I was a happy customer,” says one client.

Reimo Hammerberg heads the banking and finance team, and is described as “an

excellent lawyer” by one banking client. Hammerberg led on a deal providing export finance to a company buying three ferries from a Norwegian shipyard.

Hammerberg also led on restructuring of the collateral \$62 million credit facility to an oil company. The deal involved securing the client’s status and changing the pledger of shares and bonds. Hammerberg also led on Estonian aspects of a \$200 million credit facility provided by a Norwegian bank to a global manufacturer as part of a reorganisation.

Toomas Prangli is the other leading light at Sorainen and he heads the M&A side of the firm. He led on a deal that is typical of M&A work now – advising Atria on its purchase of meat processing companies Woro Kommerts and Vaste-Kuutse Lihatoostus.

Leading lawyers

Reimo Hammerberg
Toomas Prangli

Other ranked firms

Eversheds Ots & Co has been visible in the R&I market, while one peer notes that the firm “has a good banking practice”. Managing partner Maivi Ots is considered the firm’s leading light.

Clients appreciate **Glikman & Partnerid**’s business and transaction focus. “The firm’s work has been very professional, very accurate and I think all aspects are good,” says a client.

In banking and finance the firm has received a steady stream of work from Danske Bank, which uses the firm as its legal adviser for Estonia. On the M&A side Glikman helped prepare nine subsidiary companies of Kalev for sale, including a restructuring of the group and the creation of two distinct groups of companies.

Paul Varul is a domestic-focused firm which the market rates highly. Peers note the firm’s expertise and visibility in R&I matters. For banking and finance, Ants Mieland leads the team that counts SEB and Gild Bank as clients.

On the M&A side Paul Varul represented Kodukolde Kinnisvara, the sole shareholder in meat processing company Vastse-Kuuste Lihatoostus, on the sale of the meat processor to the Atria Group. The deal was completed in August 2008.

Tamme & Otsmann is a “small firm that has some good clients and is able to do transactional work” according to one peer. Name partner Tonis Tamme is a solid M&A lawyer according to the market.