

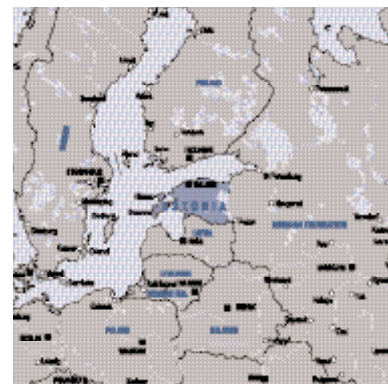
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Recent changes in Estonian contract law

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One of the most important changes in Estonian contract law took place on July 1 2002 when the Law of Obligations Act, General Part of the Civil Code Act, and Private International Law Act entered into force. While multiple provisions of the General Part of the Civil Code Act and Private International Law Act could also be found in previously valid Acts, the Law of Obligations Act entirely replaced the Civil Code of the Estonian SSR that had been in force since 1965. The Civil Code, dating back to the Soviet era, had become hopelessly limited in its ability to regulate transactions, and the Law of Obligations Act introduced revolutionary changes, especially in respect of the conclusion and execution of transactions and the regulation of certain specific transactions. These principles had long been applied in contracts between parties to international and local M&A transactions, but legislation did not support enforcement of such contracts and their interpretation in the case of any dispute.

Now a solid foundation has been laid for the development of uniform court practice, and the general principles of Estonian contract law are similar to the principles generally valid in Europe. The Principles of European Contract Law developed by the European Commission and published in 1995, as well as the Principles of International Commercial Contracts developed by the International Institute for the Unification of Private Law (Unidroit) and published in 1994, served as the basic models for the development of the Law of Obligations Act. The Civil Codes of Germany, the Netherlands, Switzerland, Russia, Louisiana, Quebec and Italy, and relevant Finnish and Swedish laws, were also used as models while the draft act was being developed.

The principle of party autonomy provided for in the Act, pursuant to which the parties are by mutual agreement entitled to divert from the regulation provided for by law, should be considered as a considerable innovation. Options for diversion from the law are limited, however, predominantly in respect of provisions relating to consumer protection and also in respect of contracts that are in conflict with good practice and public order or that would violate fundamental rights of the person.

Besides the principle of party autonomy, the principle of freedom of contract contained in the Act is also important, especially since the effectiveness of such principle under the earlier Civil Code was dubious. Now, the principles of good faith and reasonableness are of central importance when assessing parties' behaviour in a transaction. In any dispute, the parties and the court should assess how a reasonable person would have implemented the given obligation in a similar situation.

The fact that the Act prescribes few specific time limits will probably cause some confusion to begin with, but as far as development of relevant court practice is concerned,

this solution – which is based on common sense – should be viewed as a positive step.

The regulation of pre-contractual negotiations, with the option to claim for any damage caused by behaviour in bad faith (*culpa in contrahendo*) is very important at the closing of an M&A transaction. The importance of the provision lies in fact that in such cases a letter of intent is not always prepared. The Act requires that persons conducting pre-contractual negotiations shall take reasonable account of each other's interests and rights. Any data presented to the other party during the course of negotiations must be true, and the holder of data must present such data to the other party if material interest in such data may be presumed from the other party as far as the aim of the contract is concerned. The obligation to keep such data confidential lies with the parties, and they may not use such data in their own interests.

Failed negotiations do not automatically result in legal actions between the parties. However, if one of the parties has conducted negotiations in bad faith, mainly without intention to arrive at a successful transaction, the other party will be entitled to claim for damages.

The new General Part of the Civil Code Act that entered into force on July 1 2002 replaces the General Part of the Civil Code Act that had been in force since 1994. The Act does not establish any new regulation as far as basic principles are concerned, but the adoption of the new Act was mainly necessary because of the Contracts and Off-Contract Obligations Act, the enforcement and application of which presumes comprehensive amendment of the General Part of the Civil Code Act.

The Law of Obligations Act establishes regulation of contracts of sale, barter agreements, gratuitous contracts, factoring contracts, lease contracts, commercial lease contracts, capital leasing contracts, licence agreements, franchise contracts, loan and credit agreements, insurance contracts, authorization agreements, contracts for services, brokerage contracts, agency contracts, contracts of carriage and transfer of securities as separate kinds of contracts, as well as several other less important kinds of contracts. Obligations that may arise outside the contract, such as causing damage and unjust enrichment, are now highly regulated.

The expiration provisions of the Contracts and Off-Contract Obligations Act have also been extended, and now contain specific provisions regulating, among other things, the expiration of any obligations arising from various debt relationships.

In the case of M&A transactions, of particular note are the provisions regulating conditional transactions, the practical significance of which become evident in the case of ownership reservations. Making the transfer of the right of ownership of the object conditional upon the payment of the purchase price will invalidate any transaction where the seller has transferred the object of a transaction that was concluded with a suspension condition.

In conclusion, it is impossible to overestimate the importance of the new legislation in terms of its effect on the regulation of Estonia's developing economic environment. The legislation creates a solid foundation for the development of a legally certain and unambiguously comprehensible business environment.

Banking

Recommended firms

Raidla & Partners

Law Office Tark & Co

Law Office of Lepik & Luhaäär LAWIN

Luiga Mugu & Borenius

Sorainen Law Offices

Teder & Rask

Alvini Advokaadibüroo

Hedman Osborne Clarke Alliance

Heta Law Offices

Hough Hübner Hütt & Partners

Capital markets

Recommended firms

Luiga Mugu & Borenius

Raidla & Partners

Law Office Tark & Co

Heta Law Offices

Law Office of Lepik & Luhaäär LAWIN

Lohmus & Haver Viiseman

Sorainen Law Offices

Teder & Rask

Aivar Piltv

Hedman Osborne Clarke Alliance

Mergers and acquisitions

Recommended firms

Law Office of Lepik & Luhaäär LAWIN

Raidla & Partners

Law Office Tark & Co

Heta Law Offices

Luiga Mugu & Borenius

Sorainen Law Offices

Teder & Rask

Hedman Osborne Clarke Alliance

Mody & Hääl Glimstedt

Project finance

Recommended firms

Luiga Mugu & Borenius

Raidla & Partners

Law Office Tark & Co

Law Office of Lepik & Luhaäär LAWIN

Sorainen Law Offices

Teder & Rask

Law Office of Lepik & Luhaäär LAWIN

Lawin is the third alliance of Baltic law firms to come together over the last year. This one combines the expertise of Lepik & Luhaäär from Estonia with Klavins & Slaidins from Latvia and Lideika Petrauskas Valiunas & Partners from Lithuania. Both of Lepik & Luhaäär's new partners are well-respected firms in their own jurisdictions; Lideika is one of Lithuania's oldest and best-established collections of lawyers.

Lepik & Luhaäär itself was the first private law office to be founded after the country's independence in 1990. It comprises 20 lawyers in the capital Tallinn and is the Estonian representative of the Lex Mundi association of law firms.

The firm is particularly recommended as a source of legal advice for international corporations with interests in Estonia. It has advised on the establishment of subsidiaries in the country for many US and European companies as well as advising on export and franchising contracts under Estonian law.

Key contact partners

Peeter Lepik

Toomas Luhaäär

Luiga Mugu & Borenius

A "strong name for capital markets transactions", Luiga Mugu & Borenius is a young, dynamic firm that is growing fast. Last year it hired three associates – Aivar Taro, Maksim Greinoman and Ave Piik – to bring the team up to 10 lawyers in Estonia's capital, Tallinn. The two name partners, Sten Luiga and Margus Mugu, are both highly recommended by their clients and competitors.

Like contemporaries Raidla, Sorainen and Lepik & Luhaäär, Luiga & Mugu has looked to expand its reach across the Baltic rim and into Finland. It opted for a pact with Finnish firm Borenius & Kemppinen, and merged with its Tallinn office. Through Borenius the firm can now offer clients legal advice on Finnish and Latvian law as well as Estonian matters.

The firm has always had a solid reputation for capital markets and project finance work – it is one of three firms that together account for around 90% of capital markets deals in the country. But over the last couple of years it has also impressed in mergers and acquisitions work, with several large deals. It began with advice to the Sylvester Group, the largest forest group in the Baltic States, on its acquisition by Stora Enso. At around €130 million (\$146 million) it was the biggest deal of 2002 and the largest in Estonian history. More recently the firm advised on the takeover of one of Estonia's largest textile producers, counselled a group of Russian investors on the purchase of an oil share plant and advised Cramo AB on several acquisitions of large construction companies in Estonia.

Key contact partners

Sten Luiga

Margus Mugu

Leading lawyer

Sten Luiga

Raidla & Partners

On April 4 2004 Raidla & Partners agreed to merge with three other firms – Roschier Holmberg in Finland, Lejins Torgans & Vonsovic from Latvia and Lithuanian firm Norcouc & Partners. The combined firm has renamed itself RoschierRaidla and now offers advice to clients across all four Fenno-Baltic countries, with a staff of over 150 lawyers. Roschier Holmberg and Lejins Torgans & Vonsovic are leading firms in their respective jurisdictions, as the Finnish and Latvian sections of the *IFLR 1000* demonstrate – both firms are ranked among the top firms in every practice area.

As for Raidla itself, the firm is one of Estonia's strongest, again ranked in the first tier for every area of work. Clients call the firm's services "first class" and particularly praise

name partner Jüri Raidla: “He is a fantastic lawyer and truly a star. I could gush for hours about how good he is.” Raidla is recommended for his banking and project finance work, while other leading lawyers Raino Paron and Sven Papp are recommended for capital markets and finance advice.

The firm’s banking clients include regional banks Hansabank and Nordea Bank, while in capital markets it has advised several corporates on offerings in the Estonian market, including Tallink Grupp, Estonian Cell and Sillamäe Sadam. It also acted for Tallinna Vesi on an €80 million (\$90 million) loan from the EBRD and Eesti Energia on a €150 million loan and a €200 million bond issue. Raino Paron has worked on the Republic of Estonia’s capital markets issues, including a €100 million bond issue where he advised lead manager Credit Suisse First Boston.

Recent mergers and acquisitions deals include advising Telia Sonera on a cash offer for the shares of Eesti Telekom, while the project finance department has been busy advising Coal Terminal on the development of a dry bulk terminal in Muuga port.

Key contact partners

Sven Papp
Raino Paron
Jüri Raidla

Leading lawyers

Sven Papp
Raino Paron
Jüri Raidla

Sorainen Law Offices

Sorainen was one step ahead of its rivals on the trend towards capabilities across Finland and the three Baltic states. Over the last few years it has gradually expanded into four fully-fledged offices in the capitals of each country, with a staff of 43 lawyers. The Estonian branch accounts for 19 of these and has grown over the last year, with the hiring of partner Pekka Puolakka from law firm Sarvi & Koponen and the recruitment of three other associates, one from rival Lepik & Luhaäär.

Law Office Tark & Co

One of the best-established and respected firms in Estonia, Tark & Co is the only firm apart from RoschierRaidla to be ranked in the top tier for every practice area covered by the *IFLR1000*. Clients describe the firm as “high on expertise” and “good at relationship-building”.

Hannes Vallikivi is the firm’s star lawyer, rising above his equally accomplished partners purely on the number of practice areas in which he is recommended. The head of the banking and finance team, he is responsible for banking advice to Deutsche Bank, Norddeutsche Landesbank and Fidelity Investments, as well as capital markets and project finance work. The firm includes JP Morgan, Barclays and

Franklin Templeton among its capital markets clients and worked on a €1.5 billion (\$1.8 billion) MTN programme and a €1 billion commercial paper programme for Hansabank last year. In project finance the firm was involved in the financing of two shopping centres – Linstow Ülemiste and Viru Centre – and advised HypoVereinsbank on a €100 million loan to Estonian Cell.

Other accomplished partners include Risto Vahimets and Aare Tark. Vahimets worked on the firm’s three standout mergers and acquisitions deals last year: the acquisition of Estonian Air by SAS, the takeover of Preatoni Pank by Nikolaos Sarros and Rein Kuusmik’s sale of Repo.

Key contact partners

Aare Tark
Risto Vahimets
Hannes Vallikivi

Leading lawyers

Aare Tark
Risto Vahimets
Hannes Vallikivi