

COMMERCIAL LAW

No. 27

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EUROPEAN UNION

EU JUDGEMENT ENFORCEABLE
IN BALTICS

From 01.05.2004 onwards the Council Regulation (EC) No 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters will be effective and directly applicable in the Baltic States.

The purpose of the Regulation is, firstly, to have common rules on jurisdiction and, secondly, to attain the objective of the free movement of judgments in civil and commercial matters within the European Union.

As a main rule, persons domiciled in a Member State shall (regardless of their nationality) be sued in the courts of that Member State. According to the Regulation, if at least one of the parties is domiciled in a Member State, it is possible to agree that court (or courts) of a Member State have jurisdiction to settle any disputes in connection with the particular legal relationship. Such an agreement on jurisdiction must be concluded in writing. Some courts, however, have an exclusive jurisdiction, which cannot be contracted out. For example, in proceedings concerning real estate the courts of the Member States, in which the property is situated, have an exclusive jurisdiction. The same applies to proceedings concerned with the registration or validity of patents, trademarks, designs or other similar rights. The court of the Member State in which the deposit or registration has been applied for or has taken place has an exclusive jurisdiction over such disputes.

In relation to insurance, consumer and employment contracts, the weaker party is protected by rules of jurisdiction more favourable to his interests than the general rules provide for.

A judgment given in one Member State shall be recognized in the other Member States without any special procedure. In addition, a judgment given in a Member State and enforceable in that State shall be enforced in another Member State when, on the application of any interested party, it has been declared enforceable there by the local court or competent authority (as indicated in the Regulation).

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ESTONIA

COMPANY LAW

A new **Bankruptcy Act** (*Pankrotiseadus*) came into force on 01.01.2004 to replace a former law of the same title. The purpose of the new act is to establish the framework compatible to the present requirements and expedite the bankruptcy process. You can find an overview of the relevant aspects of the new act on the last page of this Baltic Legal Update and also on our web-page www.sorainen.com

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LAND REGISTER

An electronic database of the land register has been established in Estonia. The database is available for public on the Internet (<http://www.eer.ee/kinnistu.phtml>). In the future the database will be used as an electronic land register, which has legal effect. At the moment the electronic database exists only for informative purposes and might contain mistakes. Our few-months experience in using that database has shown that several mortgages have not been entered in the electronic database. Although currently only the paper version of the register extract, issued by the Public Title Register, is legally binding, we suggest that all owners of the registered immovables, mortgagees and others whose rights should be reflected in the land register, check whether their rights are registered with the electronic database and in case of any mistakes, inform the Public Title Register immediately.

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LAW OF OBLIGATIONS

Amendments to the **Law of Obligations Act** and related legislation (*Võlaõiguseaduse ja sellega seonduvate seaduste muutmise seadus*) entered into force on 27.12.2003 attempting to solve the mistakes made in drafting the Act, but fails to fix many of them. The amendments have no retroactive force and therefore they do not solve the problems that have already occurred.

Estonia

New Bankruptcy Act entered into force in Estonia

Latvia

Major changes in Tax Law come into force in Latvia

Lithuania

Corporate reform in Lithuania

Sorainen Law Offices

Our Helsinki office has moved!

LEGAL UPDATE

Amendments have been made to the provisions regulating the penalties and claims for performance of obligations, and the law no longer requires claiming penalties "immediately" but "within a reasonable time". The amendment follows the practice as negotiations are the first remedy in the case of disagreement, and penalty claims are filed after negotiations have failed, never immediately.

Amendments were made to the system of (late payment) interest rates, which are applied if no interest rate has been agreed between the parties. Statutory interest now equals 7% per annum until 01.05.2004 and after 01.05.2004 the interest rate of main refinancing operations of the European Central Bank: <http://ecb.int/home/ecbinterestrates.htm>, (2.5% per cent until 01.07.2004); statutory late payment interest equals statutory interest, plus 7% per annum.

Also, a consumer cannot be demanded to pay late payment interest on overdue payments at a rate higher than the statutory interest rate.

Amendments also concern pre-emptive rights. As from 27.12.2003, it is expressly and unambiguously defined that the pre-emptive right is applicable not only to contracts of sale, but also other transfers for a fee. The amendments also concern pre-emption of movables by requiring a time period before the movable can be transferred, but the wording of the new regulation may still leave gaps to the pre-emption of movables. This will mostly affect transfers of ideal parts of movables (such as ideal parts of buildings on land which is still not privatised).

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LAW OF PROPERTY

Amendments to the **Law of Property Act Implementation Act** (*Asjadigusseaduse rakendamise seadus*) that entered into force on 20.12.2003 extend the deadline for transferring structures or parts thereof as movables from 31.12.2003 to 01.07.2006.

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MONEY LAUNDERING

A number of amendments to the **Money Laundering and Financing of Terrorism Prevention Act** (*Rahapesu ja terrorismi rahastamise tõkestamise seadus*) entered into force on 01.01.2004. Foremost, the number of persons, who are obliged to identify a person and notify the Financial Intelligence Unit about suspicious transactions, is dramatically increased (including financing institutions, currency exchange and currency transfer services, traders of precious metals, auditors and persons offering counselling services in field of accounting and taxation). In certain transactions this requirement extends to notaries, attorneys, other persons offering counselling services, and any other entrepreneurs that carry out or assist a transaction where he receives or pays in cash an amount exceeding EEK 100,000 or by wire transfer EEK 200,000.

According to the amendments, the obligation to notify does not apply to notaries, auditors and attorneys when issuing legal opinions or representing a person in court proceedings.

The amendments provide that businesses offering currency exchange services are obliged to register themselves with the registry of economic activities by 15.04.2004.

From 01.01.2004 credit and financial institutions should annually repeat checking of data used for identification of a person. For credit and financial institutions (and their managers) a breach of money laundering rules is subject to criminal sanctions. Given that the definition of financial institutions is very wide (including e.g. holding companies) it is recommendable that most entrepreneurs check carefully their obligations arising out of this law.

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PUBLIC PROCUREMENT

According to the **Act Amending the Public Procurement Act** (*Riigihangete seaduse muutmise seadus*), entered into force on 01.01.2004, the domestic value thresholds are increased up to the amount of EEK 300,000 for purchasing goods or contracting services (previously EEK 100,000) and up to 2 MEEK for contracting construction work (previously EEK 500,000). The value of procurement contract is now calculated without the value added tax.

The provisions regulating the organisation of public procurement in case the procurement's value is below the threshold (the buyer is obliged to use the method of tenders, requesting tenders at least from three different tenderers) were added to the Public Procurement Act.

Pursuant to amendments, the purchase of health and social services, which according to previous enactments was not subject to public procurement, is now subject to public procurement provisions.

The amendments also establish the right to buy services without public procurement from a person who has exclusive right to provide certain services under the European Union legislation.

The information regarding the public procurement must be available to all market participants. In respect of public procurements exceeding the international value thresholds, the public procurement register will forward the respective data to the Official Journal of the European Communities.

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TAX LAW

Amendments to the **Income Tax Act** (*Tulumaksuseadus*) entered into force on 01.01.2004. The main amendments, which primarily concern private persons, are the elaboration on taxation of the income of non-residents, increase of the basic tax

exemption of resident private persons to EEK 16,800 per annum, and decrease of the 26% income tax rate to 20% over three years starting from 2005. The procedure for taxation of Estonian residents' income from employment was also amended so that it is now exempted from Estonian income tax for residents who have stayed abroad for 183 days during a 12 month period and have already paid income tax in the foreign country.

In respect of legal persons, income tax will not apply to fines imposed pursuant to law, the value of seized property, and charges for special use of water and pollution charges, as these are considered business-related expenses. Also, the Act provides for several derogations, which will apply from accession to the EU (e.g. principles of the directive on parent companies and subsidiaries). However, the highly important directive 2003/49/EC on interest and royalty payments, which amongst other things exempts interests on loans between related undertakings from withholding tax, has not been harmonised.

The new **Value Added Tax Act** (*Käibemaksuseadus*) entering into force on 01.05.2004 transposes the principles applicable to the EU intracommunity trade and related reporting. These concern, above all, Intrastat declaration and recapitulative statement.

The second major change arises from the EU Sixth Directive on value added tax, according to which VAT (in Estonia 18%) is applied to the first purchase of new structures, residential land, and apartments. VAT is payable immediately upon financial lease of cars and immovable property. Tax-free trade on board of ships and airplanes will be abolished after 01.05.2004, implying that at least 18% VAT will apply to the goods sold on board of these means of transport.

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LATVIA

CUSTOMS LAW

As of 26.11.2003, the **International Convention on the Harmonization of Frontier Controls of Goods** is effective in the Republic of Latvia. To facilitate the international circulation of goods, the convention provides for a cut-down on formalities, as well as number and duration of controls, especially in the coordination of the control procedures and their application methods on the national and international scale. The parties to the convention undertake to organise the activities of the customs service and other control institutions in a maximally harmonised way.

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FINANCE LAW

On 01.01.2004 the new **Financial Instruments' Market Law** ("Finanšu instrumentu tirgus likums") came into effect to replace the previously effective Securities Law as of 1995. The new law introduces material amendments to the definition of a publicly traded financial instrument, and henceforth only those instruments will be deemed to constitute publicly traded financial instruments that are placed on the regulated market, e.g., on the Riga Stock Exchange. Hereby Latvian legislation in the securities market and related activities will be harmonised with the EU law. From now on, annual accounts and reports on material regulations to the Financial and Capital Market Commission do not need to be submitted by those issuers of securities that trade their securities publicly, but the public trading of such securities has not been prescribed for regulated markets. The new law provides for a unified treatment of the participants of the financial instrument market in respect of carrying out certain activities subject to licensing and supervision. We expect that the law will improve the Latvian securities market. Finally, the new law will let the public companies to reregister themselves into the private companies. Therefore, the number of the "quasi" public companies (where the biggest shareholder owns more than 90% of shares) will diminish substantially.

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MONEY LAUNDERING

On 01.02.2004 amendments to the **Law On Prevention of the Laundering of the Proceeds from Crime** ("Par noziedzīgi iegūtu līdzekļu legalizācijas novēršanu") take effect. The amendments provide that the law will now apply also to public notaries, attorneys at law, their employees and self-employed lawyers, when they assist their clients in planning or effecting real estate or company sales and purchase transactions, in the client's cash, securities and other fund management, opening and maintenance of various accounts, placement, operation or administration of deposits for establishment of companies, establishment, administration or management of trusts, companies and similar structures, as well as when they represent the client or act on their behalf in financial transactions or transaction with real estate, except for the cases related to the representative's or defendant's functions within court proceedings.

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PACKAGING

On 01.01.2004 the new regulations **On Applying Deposit System to Reusable Packaging** ("Par depozīta sistēmas piemērošanu atkārtoti lietojamam iepakojumam") came into force. According to these regulations consumers will have the possibility to deliver reusable packaging (e.g., beer and soda bottles) and receive a refund. The regulations provide for a 2-

year transitional period, to allow the stores to prepare for the compliance with the new requirements. The regulations stipulate that the deposit system for reusable packaging is to be fully implemented at the moment when the manufacturers have registered themselves and have started selling goods in packaging that is compliant with the provisions incorporated in the regulations.

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TAX LEGISLATION

Pursuant to the amendments to the **Law On Corporate Income Tax** ("Par uzņēmumu ienākuma nodokli"), as of 01.01.2004 the corporate income tax rate has been decreased from 19% to 15%. The amendments declare invalid the tax allowance previously granted to companies and enterprises manufacturing hi-tech and software products. Starting with the taxation period of 2004, domestic companies are subject to the law provisions laying down the regulation for taxation in the case of company reorganisation. The law aims at preventing the capital increase resulting from asset transfers, performed in the course of reorganisation being taxed with corporate income tax.

In accordance with the amendments to the **Law On Private Income Tax** ("Par iedzīvotāju ienākuma nodokli"), effective as of 01.01.2004, private income tax will not be applied to dividends received from companies incorporated in the EU member states.

At the end of 2003, there were two amendments passed to the **Law On Value Added Tax** ("Par pievienotās vērtības nodokli"). The first of the amendments prescribe a new definition of the concept "inland" stating that "inland" is the customs territory of the Republic of Latvia, namely, including the customs warehouses, tax free zones and shops. The second amendments to the law cancel the reduced 9% tax rate and introduce, instead, a VAT of 5%. The reduced rate will be applicable as of 01.05.2004 (excluding, though, certain deliveries of the media, which will continue to be subject to 18% tax rate).

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LITHUANIA COMPANY LAW AND PUBLIC REGISTERS

At the very beginning of 2004, the Lithuanian company law, as well as the company registration system underwent essential changes. The necessity to amend the system was affected by the forthcoming EU accession and the need to harmonize the legal provisions regulating the company law and the registration procedures of legal persons with the requirements of the Civil Code.

Material changes have been introduced to the Lithuanian system of public registers.

The Government adopted a resolution establishing the **Commercial Register** (*Dėl Juridinių asmenų registro įsteigimo ir Juridinių asmenų registro nuostatų patvirtinimo*). This resolution is aimed at simplification of the registration procedure of the legal persons as well as at ensuring the protection of the interests of third parties. According to the newly established system, all public and private legal persons, including limited liability companies, personal enterprises, associations, state enterprises, religious communities etc., must be registered with the Commercial Register. From the start of operation of the Commercial Register a number of provisions of the Civil Code came into effect.

The new registration system of legal persons provides for the following major novelties:

1) Company names now do not have to be registered with the State Patent Bureau. The Commercial Register has been authorized to check the conformity of the name of a legal person to be registered with certain legal requirements;

2) In order to become sponsorship donors legal persons are required to register the status of a sponsorship donor with the Commercial Register;

3) It has become possible to register a procurator (general power of attorney) with the Commercial Register;

4) Companies are required to submit their annual financial statements to the Commercial Register, therefore the annual financial statements of companies have become publicly available documents;

5) As a rule, the validity of and the compliance of the documents submitted to the Commercial Register with the legal requirements has to be verified by a notary;

6) The procedure of removal of the legal person from the Commercial Register has also been simplified. The requirement to submit to the Commercial Register the certificate issued by the State Tax Inspection, a bank, the Ministry of Environment and the territorial customs office has been abolished.

All information and documents of the Commercial Register listed in the above-mentioned Government resolution are public, therefore the interested persons are entitled to access them.

The reforms also involved a change in the institutions managing the registry. The registrar of the Commercial Register is the Centre of Registers State Enterprise with its branches established in 10 county centres of Lithuania.

The Commercial Register started functioning on 01.01.2004, however, its operation is still hindered by a number of problems including the lack of practice and certain technical problems.

The Government adopted the Resolution on the **Fees for the Registration of Legal Persons and the Access to the Registration Data** (*Dėl Atlyginimo valstybės įmonei Registrų centras už juridinių asmenų, filialų ar atstovybių registravimą, duomenų pakeitimų registravimą ir naudojimąsi juridinių asmenų dydžių duomenimis bei informacija dydžių patvirtinimo*), whereby the company registration fees have been decreased. The Resolution came into force on 01.01.2004. According to the Resolution, the fee for

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the registration of a limited liability company amounts to LTL 120 (approx. EUR 35) and the fee for the registration of the branch or the representative office of a foreign legal person amounts to LTL 100 (approx. EUR 29).

However, the notary fees with regard to registration of legal persons have been increased. According to the order of the Minister of Justice as of 23.12.2003, the fee payable to the notary public for the verification of the compliance of the founding documents of the limited liability company with the legal requirements amounts to LTL 350 (approx. EUR 100).

Essential amendments were introduced to the Lithuanian **Company Law** (*Akcinių bendrovių įstatymo pakeitimo įstatymas*). The provisions of the Company Law have been harmonized with the EU law requirements and with the Civil Code. The law has been effective since 01.01.2004.

The regulatory sphere of the law has been extended by including the restructuring of the companies, the establishment of the branches of foreign companies and the termination of their activities.

The new version of the Company Law includes a number of new provisions, including the following:

1) The maximum number of the shareholders has been increased from 100 (as stipulated in the previous version of the Company Law) to 250;

2) The requirement for a public limited liability company to have at least one collective body (Supervisory Board or Management Board) has been abolished;

3) The required ratio of the equity capital and the authorized capital of a company has been changed. The law stipulates that in case the amount of the equity capital of a company has become less than 1/2 of the authorized capital specified in the Articles of Association (according to the previous version of the law the ratio was 3/4) measures have to be taken to correct the situation;

4) The prohibition for the private limited liability companies to issue debentures has been abolished. Further, the private limited liability companies are entitled to buy up a limited amount of their shares.

The law does not require the companies established before the 01.01.2004 to register the new version of their articles of association. However, in case of contradiction between the provisions of the articles of association and the Company Law, the latter prevails.

On 06.11.2003 the Parliament adopted the **Law on Personal Enterprises** (*Individualių*

jmonių įstatymas). The law came into effect on 01.01.2004. According to the law, only natural persons are entitled to establish personal enterprises and a personal enterprise may have only one owner. Furthermore, the law prescribes that the owner of a personal enterprise may have only one personal enterprise. Whereas this provision is a novelty in the Lithuanian company law, the law provides for the obligation of the owners of two or more personal enterprises to reorganize their personal enterprises by merger or to continue only one personal enterprise by restructuring, transferring or liquidating the remaining within 24 months from the day the law comes into force, that is by 01.01.2006.

The activities of a personal enterprise are governed by its bylaws, which came into effect from the moment of registration thereof with the Commercial Register.

The managing body of a personal enterprise is the head of a personal enterprise. The owner is deemed to be the head of a personal enterprise, unless the bylaws of a personal enterprise provide otherwise. The owner of a personal enterprise is entitled to appoint another person to the position of the head of a personal enterprise.

According to the provisions of the law, the personal enterprise acquires ownership rights to the property transferred to it by the owner; therefore the property of a personal enterprise is separated from the property of the owner. However, in case the property of a personal enterprise is not sufficient to discharge its obligations, the owner of a personal enterprise is liable for the said obligations.

The new wording of the **Law on Partnerships** (*Ūkinių bendrijų įstatymas*) was passed on 06.11.2003 and became effective on 01.01.2004. As in the previous wording of the law, the new wording provides for two types of partnerships – general partnerships (with all participants having the status of a general partner) and limited partnerships (having both general partners and limited partners among their participants). Only general partners are entitled to manage a partnership.

The joint venture agreement drafted pursuant to the requirements listed in the law is the founding document of a partnership. According to the law, the limited partners may not be parties to the joint venture agreement. Limited partners are required to enter into the limited partner agreement instead. Under the provisions of the law the general partner of a partnership is forbidden from being the owner of a personal enterprise or the general partner in another partnership. Therefore the law stipulates that:

i) A person, who is a general partner in two or more partnerships, is obliged to

preserve general partnership in only one of such partnerships within 18 months following the entry into force of this law;

ii) A person being simultaneously the general partner of a partnership and the owner of a personal enterprise is required to preserve his/her membership in only one of the legal persons with unlimited civil liability within 18 months from the day the law comes into effect.

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EMPLOYMENT LAW

The new version of the **Law on Social Insurance of Occupational Accidents and Occupational Diseases** (*Nelaimingų atsitikimų darbe ir profesinių ligų socialinio draudimo įstatymo pakeitimo įstatymas*) was adopted on 11.11.2003. The law provides for the differentiation of the tariffs of social insurance contributions for occupational accidents. The tariffs of the social insurance contributions are established for every assessor individually according to the number of accidents and the level of the occupational disease morbidity in a certain company. The law came into effect on 01.01.2004 with certain exceptions.

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INTERNATIONAL AGREEMENTS

The Agreement on Conformity Assessment and the Acceptance of Industrial Products between Lithuania, Iceland, Liechtenstein and Norway was signed on 30.01.2003. On 01.11.2003 the Parliament adopted the Law on the Ratification of the mentioned Agreement.

The purpose of this Agreement is to extend the area of the more favourable conditions for the development of business, to save the funds and the time of exporters as well as to reduce protectionism. This Agreement came into force on 01.12.2003.

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TAX LAW

Following the obligations of Lithuania to the EU to increase excise duties on certain products, the excise duties on cigarettes, petrol, the substitutes and additives thereof, burning oil, gasoline, the substitutes and additives thereof have been increased. On 01.01.2004 the amendments to the **Law on Excises** (*Akcizų įstatymas*) took effect.

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Contributed by Lea Liigus, Estonia; Julija Jerneva, Latvia; Justina Gutauskaitė, Lithuania. Edited by Girts Ruda, Latvia.

Our Helsinki office has moved!

We are pleased to announce that Sorainen Law Offices Helsinki office has moved to its new premises in
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Please note that Helsinki office has new contact numbers as well:

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We look forward to seeing you in our new office!

NEWS IN SORAINEN LAW OFFICES

Sorainen Law Offices:

2003 was successful for Sorainen Law Offices

2003 was the best and busiest year ever for Sorainen Law Offices. We served more than 1000 clients, handled more than 2000 cases and had an especially large amount of Pan-Baltic assignments from our clients who operate in the whole region. We employed 10 new lawyers, being 40 lawyers in total today. Mr. Pekka Puolakka, a Finnish Attorney-at-Law, joined us as a partner as of 01.01.2004. He started our Vilnius office in 1999, but moved back to Finland three years ago and practiced M&A and financing law in a highly regarded Finnish law firm Sarvi&Koponen. Among others, Mr. Puolakka will be in charge of Sorainen Law Offices' operations in Finland. Mr. Agris Repss, a Latvian Attorney-at-Law, who has been working in our Riga office since 2000 was invited to become an associate partner. He will be in charge of our Pan-Baltic Litigation & Arbitration as well as IT & Telecommunications Legal Working Groups.

Seminars

The Baltic Business Law Seminar organized by Sorainen Law Offices was successfully held on 27 November 2003 in Vilnius, Lithuania. 75 participants attended the seminar, our clients and partners among them. The presentations given at the seminar reflected the topics of EU funds and post-accession issues (Rupinder Singh, a former EU official and advisor to governments and business); cartels and cartel enforcement after 1 May 2004 (Juhani Siira, Sorainen Law Offices in Vilnius); bankruptcy proceedings in the Baltics (Girts Ruda from Sorainen Law Offices in Riga); pan-Baltic mergers and acquisitions (Toomas Prangli and Kestutis Adamonis, Sorainen Law Offices in Tallinn and Vilnius respectively); business environment in Lithuania (Gintaras Steponavicius, Parliament of the Republic of Lithuania); taxation in the Baltics (Andrius Kavoliunas, Deloitte & Touche) and joint ventures (Harry Piel, Sybase Baltic).

Tallinn office: Seminars

On 18.12.2003 legal counsel Karin Madisson made a presentation entitled "What manager should know about the commercial code and bankruptcy law?" at the Äripäev seminar "What kind of agreement protects board members?".

On 11.12.2003 our Tallinn office personnel were the exclusive speakers at the conference "Risks of the Board Members", organised by Kontakt Konverentsid OÜ and moderated by

legal counsel Reimo Hammerberg. Legal counsel Karin Madisson made the presentation on risks of board member liabilities and partner Toomas Prangli gave an overview of M&A activities and regulations in Estonia.

On 11.12.2003 and 12.12.2003 managing partner Aku Sorainen gave a presentation "Doing business in Estonia" both in Seinäjoki, Finland and Tampere, Finland.

On 05.11.2003 partner Toomas Prangli gave a presentation "Key Environmental Issues in Baltic M&A Deals" at the Insko seminar "Mergers and Acquisitions - Environmental Issues and Liabilities" held in Helsinki.

On 04.11.2003 partner Kaido Loor and legal counsel Reimo Hammerberg made presentations in the conference "EU Implications on Real Estate and Construction - Should I Invest Before or After Estonia's EU Accession?" organised by the Estonian Trade Council. Kaido Loor lectured on "VAT on the initial sale of land" and Reimo Hammerberg on "Restrictions on Acquisition of Immovables in Estonia".

Articles

Two articles "New bankruptcy law in Estonia", written by legal counsel Karin Madisson and "Important changes in obligations law", written by legal counsel Konstantin Kotivnenko were published in the magazine "The Journal of Estonian Economy" in No. 11/2003 and 10/2003 respectively.

Legal counsel Paul Künnap from Helsinki office gave a review of the process and terms of accession and the practical changes arising from accession in his article "Final preparations for the Baltic accession to the European Union". This article was published in the business magazine Northern Enterprise December 2003 issue.

The article "VAT on the initial sale of land" written by Konstantin Kotivnenko was published in the publication of the American Chamber of Commerce in Estonia Volume 8 Number 3.

Legal counsel Risto Agur described the questions related to branches in Estonia in his article "The legal regulation of branches needs to be specified" published in the 24.11.2003 issue of the Estonian business newspaper Äripäev.

Karin Madisson continued analysing the issues connected with management board member agreements by writing an article "Written contract is more advantageous to management board member", which was published in the Estonian business newspaper Äripäev on 05.11.2003.

The aforementioned articles can also be found at our webpage www.sorainen.com

Riga office: More members of the Bar in Riga Office

Our Riga office legal counsel Daimars Skutans has become a member of the Latvian Bar. During the last year our

offices have seen an increased demand for assistance in various litigation matters. Thus the new status of Mr. Skutans will help us to provide even higher quality service to our clients while representing them to any court instances.

Articles

Attorney-at-Law Girts Ruda gave two interviews: "Finnish law offices follow their clients" and "The EU protects from the insolvent clients", which were published on 17.12.2003 in "Diena Bonnier" and on 01.12.2003 in Lithuanian newspaper Verslo linios respectively.

An article "Banks to take account of the growing risks" written by Attorney-at-Law Girts Ruda was published in The Baltic Times, issue October 23-29, 2003.

The aforementioned articles can also be found at our webpage www.sorainen.com

Vilnius office:

Articles

The article "Principles of the Arbitration Procedure" written by partner Renata Berzanskiene was published on 15.11.2003 in issue 20 of the magazine "Eurolawyer".

The article "The Legal Aspects of Baltic Real Estate Market" written by Attorney-at-Law Juhani Siira was published in issue No. 5 (Autumn 2003) of the magazine "Nordicum".

Attorney-at-Law Marius Urbelis described the main aspects of corporate immigration in his article "Corporate Immigration of the European Union Citizens to Lithuania", which was published in issue No. 8 (Autumn 2003) of the BCC Paper.

The article "How Will Customs Work Once Lithuania is in the European Union?" written by Justina Gutauskaitė was published in issue No. 8 (Autumn 2003) of the BCC Paper.

Attorney-at-Law Juhani Siira gave an overview of the possibilities to protect the business secrets in the article "Legal Protection of Business Secrets in Lithuania", published in the December issue No. 3 of ACC News.

The aforementioned articles can also be found at our webpage www.sorainen.com

New hires

On 02.01.2004 Ms. Vaida Katkute joined our Vilnius office as a General Assistant. Vaida graduated from the Vilnius Pedagogical University in 2003, where she studied English philology. Presently she is studying the European Union Policy and Management in the Law University of Lithuania and she is going to obtain her Master's degree in 2004. Vaida speaks Lithuanian, English, German and Russian.

BRIEF INTRODUCTION
TO THE NEW
BANKRUPTCY ACT

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The new Bankruptcy Act came into force on 1 January 2004 and it replaces the act passed in 1996. The new Act substantially supplements and elaborates on bankruptcy proceedings and possibilities of compromise and rehabilitation. Additionally, the new Bankruptcy Act provides, for the first time, for the release of a debtor who is a private person from obligations.

One of the objectives of the new Act was to speed up bankruptcy proceedings and the law substantially elaborates on the terms of bankruptcy proceedings. A bankruptcy process lasts for approximately three years in Estonia, which is definitely a hindrance to economic processes in our rapidly developing economy.

One of the objectives of the Bankruptcy Act was to intensify supervision over trustees in bankruptcy. Supervision exercised only by courts has not been justified in practice, and according to the new Act, also the Ministry of Justice exercises state supervision over the activities of trustees. Additionally, the new Act provides for obligatory liability insurance of trustees with the minimum amount of not less than one million kroons per insured event.

If a legal person is permanently insolvent, the members of the management board have the obligation to file a bankruptcy petition immediately after the relevant circumstances become known. Violation of this obligation may in addition to civil liability result also in liability pursuant to the Penal Code (imprisonment of up to three years).

The new law enables a creditor who filed a bankruptcy petition with a court and who was required by the court to deposit a sum of money with the court toward the cost of bankruptcy proceedings to claim reimbursement of this sum from persons who failed to submit the bankruptcy petition on time. This should give more confidence to creditors to commence bankruptcy proceedings.

A creditor may file a bankruptcy petition with a court also if its claim is not reimbursable yet, but there is reason to believe that the claim will not be satisfied. Examples of such cases included events when the debtor has destroyed, hidden or squandered its property or made grave errors in management as a result of which the debtor has become insolvent, or has intentionally caused its insolvency in any other manner, or the debtor has notified the creditor, the court or the public of its inability to perform its obligations, or the debtor has left Estonia in order to evade performance of its obligations, or hides for the same purpose.

A very important regulation requires that a trustee in bankruptcy must in addition to newspapers give written notice of the bankruptcy to all creditors known to him or her as well as any pledgees and persons

who have obligations to the debtor. There is no such obligation only if the total number of obligated persons or creditors exceeds one hundred. In such case, only the obligation of giving written notice to creditors and foreign pledgees remains. Until today, creditors in foreign countries were practically unprotected, as they did not necessarily get information about declaration of the debtor's bankruptcy in time, and were therefore late with their claims. Creditors are required to notify the trustee of their claims not later than within two months after the date of publication of the bankruptcy notice.

Notification has substantial importance also for pledgees. If a creditor with a claim secured by a pledge fails to file a claim within the specified term, the right of security held by the creditor is deemed to have extinguished. That fact does not influence the existence of the claim, but the claim is not secured by a pledge any more and, hence, is not to be satisfied before other creditors.

A very important change is specified in § 80 (3), namely the judge participates in the first general meeting of creditors. The judge resolves any disputes that may arise in determining the number of votes on the spot by his or her oral ruling. The judge later confirms it with a written ruling, against which an appeal may be filed. The judge participates in other general meetings only if there is reason to believe that a dispute may arise in determining the number of votes.

A novel regulation is also § 139 (2), according to which, in case of sale of a debtor's immovable at an auction, all securities with compulsory selling rights (real encumbrances and mortgages) terminate. Extinguished are also those real rights, which have a ranking lower than the first real right with compulsory selling rights. The real rights that are extinguished upon an auction are deleted by the trustee from the land register without the consent of the person concerned.

Division of bankruptcy estate has always been one of the main issues of bankruptcy. The new Act has substantially changed the ranking of claims and these have been downsized in comparison with the old Act. Firstly, claims with preferential rights do not include remuneration rights any more, as Estonian Unemployment Insurance Fund satisfies those. Secondly, state tax claims are not claims with preferential rights any more, and are satisfied in the same rank with other creditors' claims that are not secured by a pledge. The fact that Tax Board's claims are not claims with preferential rights any more is a political decision that extinguishes the state's privileged position in bankruptcy proceedings, as the state has a possibility to assess the business's financial situation at a fairly early state, and thereby take immediate measures to protect its claim. Claims are satisfied according to the same principle that payments relating to bankruptcy proceedings are made first, and then the claims of the creditors are satisfied according to § 153 in the following rankings:

a) accepted claims secured by a pledge which were filed within the specified term, to the extent of the money received from

the sale of the pledged object;

b) accepted claims which were filed within the specified term (this includes also claims of pledgees that could not be satisfied with the money received from the sale of the pledged object);

c) claims which were not filed within the specified term but were accepted.

Chapter 11 covers release of a debtor who is a private person from debts. This regulation was provoked by the fact that while a legal person is released from its debts through bankruptcy proceedings, a private person remains liable for his or her obligations for 10 years, which might not be sensible. Before initiating proceedings of releasing a debtor from debts, regular bankruptcy proceedings have to be carried out, where creditors' claims are determined, the debtor's assets are sold and creditors are paid from the proceeds of sale. The court decides on the commencement of proceedings for the release of a debtor from his or her obligations upon approval of the final report on the basis of the debtor's application. If a court commences proceedings for the release of a debtor from his or her obligations, the court appoints a trusted representative at the proposal of the general meeting of creditors to whom the debtor will make payments to cover the debts.

If the debtor has generally performed his or her obligations during five years, the court may decide to release the debtor from his or her obligations. Diligent and *bona fide* debtors who have made regular payments to the trusted representative may be released from obligations in the first place. The law specifies several circumstances when the court does not release the debtor from obligations. At the request of a creditor, the court may annul the ruling on the release of the debtor from his or her obligations within one year after making the ruling if it becomes evident that the debtor has intentionally violated his or her obligations during the proceedings for the release of the debtor from his or her obligations and has thereby materially hindered satisfaction of the claims of the creditors.

Liquidation proceedings in which a legal person is deleted from the register after bankruptcy proceedings have been the main type of bankruptcy proceedings in Estonia. Yet in the world, more attention is being paid to rehabilitation proceedings that aim to heal the company and thereby continue its business activities. The new Bankruptcy Act aims to underline the importance of rehabilitation and make the compromise process more flexible. Compromise means an agreement between a debtor and the creditors concerning payment of debts and involves reduction of the debts or extension of their terms of payment.