

INSURANCE SORAINEN LEGAL UPDATE

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SORAINEN

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Dear Reader,

Here you have the Sorainen Insurance Legal Update, covering the most important developments in regulation, court practice, and insurance market in the Baltics and Belarus since our autumn edition.

Despite the impression that legal basis for insurance markets in the Baltics and Belarus is already created, nonetheless it does not remain static. This issue presents important amendments to the Insurance Activities Act in relation to the Funded Pensions Act in Estonia, measures taken to implement the Directive on qualifying holding 2007/44/EC in the Baltic States, and development of compulsory insurance for crops, cattle, and poultry in Belarus.

Insurance law develops not only with new laws and regulations: the importance of judicial precedent is also growing each year. Some recent decisions in the field of insurance contract law are reviewed in this edition.

A novelty in this issue is the article by Santa Selga, an insurance expert at our Latvian office, on recent riots in Latvia and the insurance market reaction to losses incurred during the riots. We are also very proud to announce that Sorainen has become one of the most awarded and internationally recognised regional law firms in the Baltics.

We wish you pleasant reading!

Tomas Kontautas
Partner, Head of Regional Insurance Practice Group

ESTONIA

LEGISLATION

Amendments to the Insurance Activities Act in relation to the Funded Pensions Act

On 14 November 2008 amendments to the Insurance Activities Act (the IAA) in relation to the Funded Pensions Act entered into force. We mentioned these planned amendments in our spring 2008 edition.

As from 14 November 2008, insurance companies outside the European Economic Area may not conclude pension contracts. Cross-border pension insurance contracts are also prohibited. Thus, only insurers established in Estonia may conclude pension contracts.

Processing of policyholder personal data is made more liberal. The insurer may now process client personal data without the client's consent in case of death as an insured event. The amendments allow the insurer to require a third party to provide client personal data needed for performance of an insurance contract and the third party must do so without delay.

Insurance companies have more extensive notification obligations to the Estonian Financial Supervision Authority (the EFSA) in relation to the standard terms or scheme of operations of pension contracts.

From now on, assets covering technical provisions and financial obligations related to pension contracts must be separated from assets covering other technical provisions and financial obligations and other assets of the insurance company. In case of bankruptcy of the insurer, assets related to pension contracts are used to satisfy claims arising from pension contracts only. These claims will not be paid to the policyholder, but as an insurance premium to the new insurer chosen by the policyholder.

Internal rules of an insurance company must also include a regulation for separation of costs. The internal rules had to be supplemented by 1 April 2009.

Intermediaries have a specific notification obligation when selling pension contracts. The EFSA will have wider powers in relation to pension contracts and supervising a branch of an insurer from the European Economic Area.

Planned transposition of directive on qualifying holding and other amendments to the Insurance Activities Act

In order to transpose the directive on qualifying holding (5 September 2007 directive No 2007/44/EC of the European Parliament and of the Council) a draft law to amend the IAA and other laws in the regulated financial sector is under legislative procedure. The amendments clarify requirements on acquisition of a qualifying holding and enact clearer procedural rules and deadlines for the EFSA, increasing the transparency of the procedure.

Estonia

Amendments to the Insurance Activities Act in relation to the Funded Pensions Act enter into force

Latvia

Amendments to Reinsurance Law and Law on insurance companies and their supervision

Lithuania

New minimum sum insured for Insurance Intermediaries Compulsory TPL insurance

Belarus

Approval of list of crops, cattle, and poultry subject to mandatory insurance

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The draft law extends restrictions to legal and natural persons who may acquire a qualifying holding in an insurance company. From adoption of the draft, more emphasis is to be placed on the financial status and reputation of the acquirer, as well as on the reputation and experience of future management. The draft law also adds that no reasonable suspicion should exist of money laundering or terrorist financing.

More documents and information are to be filed with the EFSA about a natural person acquiring a qualifying holding and information about future managers must also be filed. Documents must be in Estonian and only with the consent of the EFSA may information and documents in another language be filed. The draft law also specifies the procedure for evaluating an acquirer of a qualifying holding, deadlines and co-operation between regulators. The seller needs no longer file information and documents regarding the acquirer with the EFSA, but needs only inform the EFSA about the intention to sell the holding and disclose the size of the holding. Compared to current regulation, the draft law lists exhaustive grounds for refusal. The final decision is made by the regulator of the acquirer.

In addition to transposition of the directive, other amendments to the IAA are planned. Regulation of the solvency margin will be amended. The minimum solvency margin will be increased respectively from EUR 3.2 million to EUR 3.5 million and from EUR 2.2 million to EUR 2.3 million. Additionally, the basis for a required solvency margin calculation will change. The amendments regarding solvency margin are expected to enter into force on 1 January 2010.

The minimum sum insured in liability insurance contracts of an intermediary is raised. Insurance coverage must be at least EUR 1.2 million for any single claim and in aggregate EUR 1.7 million yearly for all claims. Compared to current regulation, the draft law significantly increases the maximum penalty for legal persons breaching requirements of the IAA – from EEK 50,000 (EUR 3,196) to EEK 500,000 (EUR 31,956).

Amendments to the Code of Civil Procedure

Numerous amendments to the Code of Civil Procedure entered into force on 1 January 2009. Some of these are relevant to the insurance sector. The amendments add that the court may require from insurance companies information regarding the residence and other contact information of a party to proceedings or of a witness, i.e. insurance companies must provide such information. Also the regulation of jurisdiction was supplemented lightly.

Amendments to the Motor Third Party Liability Insurance Act

On 6 December 2008 amendments to the Motor Third Party Liability Insurance Act (MTPL Act) entered into force. The amendments extend the cover of MTPL insurance to accidents taking place while driving on or off a berthing passenger ferry providing regular domestic carriage services. The amendments also add that an insurer may charge an additional insurance premium for a green card applicable in countries outside the European Economic Area or Switzerland.

New Motor Third Party Liability Insurance Act

On the initiative of the Ministry of Finance, a new working group has been formed to generate principles for a new MTPL Act. The aim is to minimise discrepancies between the MTPL Act and the Law of Obligations Act. Improvements are likely to include abolishing the current principle of (termless) contract and policy and to allow compensation for traffic damage also to be paid by the insurer of the injured party.

New advisory guidelines of the EFSA

On 19 March 2009 the EFSA established advisory guidelines on the requirements to the report of a responsible actuary. The guidelines will enter into force from 1 October 2009.

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RECENT CASE LAW

Insurer must pay reinstatement value of damaged building irrespective of actual reconstruction

The Estonian Supreme Court in its judgment No 3-2-1-113-08 of 8 December 2008 gave an opinion on the basic principles of compensation for loss under property (building) insurance.

The Supreme Court held that if a building is destroyed, reasonable and necessary reinstatement costs of the building are considered damage to the policyholder. Generally, the insurer must compensate damage irrespective of how the policyholder uses the indemnity. Thus if the policyholder claims reinstatement costs, the insurer must compensate reinstatement costs even if the policyholder declares that it will not restore the building.

However, the Supreme Court indicated that if the parties to the insurance contract have clearly agreed that payment of indemnity is bound up with actual reinstatement of the insured building, then the amount may depend on how the policyholder uses the indemnity.

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LATVIA

LEGISLATION

Amendments to Reinsurance Law and Law on Insurance Companies and their Supervision

The Parliament has adopted amendments to the Reinsurance Law and amendments to the Law on Insurance Companies and their Supervision. These amendments set a more detailed procedure for carrying out prudential assessment of suitability of a proposed acquirer of an insurer or reinsurer. They also indicate more precise criteria that should be taken into account in assessment of suitability. These amendments transpose EU Directive 2007/44/EC into Latvian law.

Amendments to Law on Insurance Companies and their Supervision

Starting from 1 January 2009 a new procedure is in place for challenging decisions of the Latvian Financial and Capital Market Commission (the FCMC). In the first instance, these decisions will be subject to review by the regional administrative court before a panel of three judges. Their judgment can only be challenged in a cassation before the Supreme Court. However, review of applications submitted prior to 1 January 2009 will be carried out in the same way as before.

From 5 March 2009, differentiation of insurance premium and insurance indemnity on the basis of gender is allowed. The Cabinet of Ministers still has to approve the list of insurance products where differentiation is allowed.

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LITHUANIA

LEGISLATION

New minimum sum insured for Insurance Intermediaries Compulsory TPL insurance and minimum own capital for insurance brokerage companies

On 9 September 2008 the Lithuanian Insurance Supervisory Commission resolved to review the sum insured for Insurance Intermediaries Compulsory TPL insurance, under Article 227 of the Lithuanian Law on Insurance and Article 4 of Directive 2002/92/EC on insurance mediation. The new annual minimum sum insured for Insurance Intermediaries Compulsory TPL insurance is EUR 1,120,200 per event and EUR 1,680,300 for all events that may occur due to the policyholder's illegal activities in any year. These requirements came into force on 13 September 2008.

New minimum own capital for insurance brokerage companies is EUR 16,803. This requirement came into force on 1 January 2009.

New Rules on Compulsory Civil Liability Insurance for audit firms

On 30 September 2008 the Lithuanian Insurance Supervisory Commission approved new Rules for Compulsory Civil Liability Insurance for Audit firms.

Under the new rules the minimum annual sum insured for audit firms' compulsory TPL insurance is LTL 100,000 (EUR 28,962) per event. When the object of compulsory civil liability insurance is civil liability of the audit firm for damage caused to the contractor and/or third parties when carrying out audits in public interest entities, the minimum annual sum insured is LTL 200,000 (EUR 57,924) per event.

The new Rules on Compulsory Civil Liability Insurance of Audit firms came into force on 2 October 2008.

Requirements for reinsurance and criteria for selecting a reinsurer amended and supplemented

On 2 December 2008 the Lithuanian Insurance Supervisory Commission approved amendments and

supplements to the Requirements for Reinsurance and Criteria for Selection of a Reinsurer.

Under the new requirements, the share of premiums allocated to reinsurers of the second and third insurance class groups must be calculated without compulsory insurance types. The new requirements also establish that the insurance company can ignore certain restrictions on and requirements for reinsurance if total insurance and reinsurance premiums underwritten by an insurance company in a financial year in an insurance class, not including compulsory insurance types, or the total amount of insurance and reinsurance premiums underwritten in a financial year in all types of compulsory insurance of the insurance class do not exceed LTL 50,000 (EUR 14,481). These amendments and supplements came into force on 10 December 2008.

New version of procedure for submitting chief actuary reports to Lithuanian Insurance Supervisory Commission

On 20 January 2009 the Lithuanian Insurance Supervisory Commission approved a new version of requirements for submitting chief actuary reports to the Commission. The new requirement came into force on 30 January 2009.

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RECENT CASE LAW

Insurer has the right but not the obligation to inspect property to be insured

In civil case No 3K-3-518/2008 the Lithuanian Supreme Court decided that an insurer has the right but not the obligation to inspect property to be insured, so that the policyholder must disclose to the insurer all information held about circumstances which may materially affect the probability of occurrence of the insured event and the amount of potential loss in respect of such event (area of the building if this does not coincide with data on the public register).

Clause of insurance contract according to which the insurer has the right to refuse to pay indemnity in respect of the non-disclosed area of the building, can not be treated as surprising and consequently as void.

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BELARUS

LEGISLATION

Approval of list of crops, cattle, and poultry subject to mandatory insurance

On 12 February 2009 the President of Belarus issued Decree No 97 on Mandatory Insurance with State Support of Crops, Cattle, and Poultry in 2009.

Decree No 97 establishes insurance tariffs as to winter wheat, winter triticale, spring wheat, and other agricultural products that must be insured in 2009. Insurance tariffs as to crops are different in each of the six regions of Belarus; insurance tariffs as to cattle and poultry are the same in all regions. 95% of insurance contributions are paid at the expense of the republican fund for the support of agricultural producers, the remaining 5% at the expense of the insured.

In 2009 the rate of recovery of damages and expenses relating to reseeding crops and breeding cattle and poultry amounts to 70%, in contrast to 50% in 2008.

Mandatory insurance of crops and most valuable species of cattle and poultry was introduced in Belarus from 1 January 2008. The only insurer under this type of insurance is the largest state-owned company Belgosstrakh.

New instruments for placement of insurance reserves

The second half of 2008 marked a significant stage in development of the securities market in Belarus. A number of changes in tax and securities legislation have led to extension of the list of instruments in which reserves and own funds of insurance companies can be invested.

The first novelty relates to preferential taxation of income received from bonds issued by legal entities – residents of Belarus – within the period from 1 April 2008 until 1 January 2013.

The second novelty is the possibility of issuing so called stock bonds, i.e. bonds denominated in Belarusian rubles with a circulation period not exceeding one year, placement and circulation of which can be realized only with open joint-stock company “Belarusian Currency and Stock Exchange”. Moreover, at present banks are entitled to issue unsecured bonds, which significantly simplifies and speeds up the procedure for registration of bonds of new issues.

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INSURANCE MARKET NEWS

Transfer of business and insurance portfolio of QBE Kindlustuse Eesti AS

On 1 November 2008 QBE Kindlustuse Eesti AS, a member of the Australian QBE insurance group, transferred its insurance portfolio and operations to the QBE Insurance (Europe) Limited Estonian branch. The transfer was made as a part of the restructuring of QBE Insurance Group European Operations.

Thus, eight local non-life insurance companies (including the Estonian Traffic Insurance Fund) and six branches of non-life insurers (Gjensidige Baltic, BTA, Codan Forsikring, Euler Hermes, Fennia Mutual and QBE) are currently registered in Estonia.

Claims adjuster CHB Europe AS is declared bankrupt

On 18 November 2008 Harju County Court declared the bankruptcy of CHB Europe AS. The company

started in 2006, providing risk assessment, risk management, loss prevention and loss adjustment services on the Estonian market. The company filed its own bankruptcy petition.

Latvian insurance market in general

Total premiums paid to non-life insurers in 2008 increased by 12% to LVL 303.1 million (EUR 431.3 million). At the same time a decline took place in the non-life insurance market, with total premiums paid decreasing by 14% to LVL 52.9 million (EUR 75.3 million).

In 2008 insurers paid insurance indemnity LVL 542,000 (EUR 771,196) a day on average. From the middle of 2008 insurers are more frequently paying insurance indemnity in kind, i.e., substituting insured property with an equivalent, or repairing it. This helps reduce risk of fraud, since in case of substitution the insured is not released from obligations to finance institutions.

Insurers suffer EUR 1.9 million loss

In 2008 insurers offering motor third party liability insurance taken together suffered a loss of LVL 1.4 million (EUR 1.9 million). This is four times less than in 2007.

The First self-service insurer in Latvia

100% self-service in motor third party liability insurance and CASCO insurance is now available in Latvia. This also includes online claims filing, and allows savings of up to 25% on the insurance premium. Letakpasam.lv belongs to IF.

Licence of Baltijos garantas DUAB suspended

On 20 January 2009 the Lithuanian Insurance Supervisory Commission decided under subparagraph 11 Article 197 and subparagraphs 2,7 paragraph 11 Article 198 of the Lithuanian Law on Insurance to suspend part of the licence of Baltijos garantas DUAB covering: accident insurance, sickness insurance, land vehicle (other than railway rolling stock) insurance, ship (sea and internal waters) insurance, property insurance against fire and natural forces, property insurance against other risks, liability arising out of the use of motor vehicles operating on land, liability arising out of use of ships (sea and internal waters), general liability insurance and financial loss insurance classes.

The decision is effective as of 2 February 2009. Additionally, the Commission decided from 1 March 2009 to suspend Baltijos garantas DUAB license, leaving the right to pursue insurance brokerage and reinsurance brokerage business.

This decision was based on the fact that Baltijos garantas DUAB has still not developed the required amount of the guarantee fund of not less than EUR 3.2 million, which should have been in place by 30 March 2007 under Article 223 of the Lithuanian Law on Insurance.

Note that these measures are temporary and if the company establishes a minimum guarantee fund by 30 March 2009, the restrictions on its activities will be removed. If not, the Commission will revoke Baltijos garantas DUAB insurance license to engage in insurance activity.

Deputy Chairman appointed to Lithuanian Insurance Supervisory Commission

On 12 January 2009, Ramunas Baravykas was appointed Deputy Chairman of the Insurance Supervisory Commission for a five-year term of office by order of the Prime Minister of 9 January 2009 No 15.

New CEO for RESO Europa ADB

The Lithuanian Insurance Supervisory Commission approved Valdas Sakalauskas as the new CEO and member of the board of RESO Europa ADB.

New members of supervisory board for PZU Lietuva

Agnieszka Smolenska-Micialkiewicz, Jolanta Kulminska-Jaroszynska, and Rafal Grodzicki were appointed as new members of the supervisory board of PZU Lietuva UAB DK and PZU Lietuva gyvybes draudimas UAB DK.

Members of supervisory board for Aviva Lietuva UAB

Adam Jacek Uszpolewicz, Marek Czeslaw Przybylski, and Maciej Krzysztof Jankowski will be members of the supervisory board of Aviva Lietuva UAB for the next term.

Authorization to reorganize insurance company RESO Europa ADB

On 3 March 2009 the Lithuanian Insurance Supervisory Commission decided to authorise reorganisation of RESO Europa ADB by incorporating it with Gjensidige Baltic ASS, effective from 28 October 2008 and confirmed that the reorganization might be completed.

New branch of another EU Member State insurance company in Lithuania

A branch of Estonian insurance company If Eesti Kindlustus AS may engage in non-life insurance activity in Lithuania from 6 November 2008. The head of the branch is Darius Antanas Kamuntavicius.

INSURERS AND RIOTS IN LATVIA

Who should pay the Bill?

"The meal" or how did it begin?

What does a pleasant dinner at a quiet restaurant have in common with a riot in Riga Old Town on 13 January 2009 when a peaceful gathering turned into destruction of police vehicles and damage to shops and buildings? The answer is simple - settlement of a bill. Let's look at the events of 13 January 2009 from the insurance perspective. Who should pay the bill for putting windows back into place?

Insurer's duty to pay

The insurance business to a certain extent is reading the future, since insurers have to find the right balance between premiums received and indemnity paid. One way to make the future more certain is by limiting liability through exceptions. After the events of 13 January 2009, one of the most well known exceptions is riots. The Latvian Association of Insurers declared that insurers need not pay indemnity, since riots are an exception listed in the Insurance Contract Law. This statement is not entirely correct, because Article 12 of the Insurance

Contract Law gives parties a choice. Thus, a list of exceptions will not necessarily include riots. At the same time, returning to planet Earth, such a possibility is unlikely due to the requirement by reinsurers to exclude liability for riots in standard terms. Another question arises – whether the events of 13 January 2009 amounted to a riot or illegal activities of third parties. i.e., a risk usually covered by insurance. No official definition of riot in Latvian law exists, or in Latvian case law to draw a borderline between the two. Thus it all comes down to the insurance policy terms and conditions and the decision of each insurer. This is one of those cases when it is impossible to find a single answer for all cases, so that each situation should be reviewed individually.

What is happening at nearby tables?

After similar events, the Estonian government asked for insurers' assistance for a rapid solution to the problem. Accordingly, insurers compensated damage, but the government undertook to repay the insurers, since the government hoped to succeed in redress claims against the organizers of the event.

Why should I pay?

Payment of each insurance indemnity increases the probability that next year premiums will increase for everybody due to higher risk. Therefore in many countries so-called ex gratia indemnity payments are forbidden, i.e., indemnity is paid to a very good client although the obligation to do so is disputable. Unfortunately, Latvian law does not give a clear answer to this. Let's assume that Insurer Y pays Client X an insurance indemnity to compensate damage caused on 13 January 2009. This creates a risk that another client of Insurer Y will have to pay more for their insurance next year just because Insurer Y did not want to spoil its relationship with one of its favourite clients. In other words, if I was at home on 13 January 2009 watching TV all evening, then why should I pay for all this?

Lessons learned

The main question in each insurance contract is: if something goes wrong, will I get my money? Therefore it is important to understand what is covered under the particular insurance policy. For example, some immovable property insurance policies do not cover broken windows if breakage is not related to any other risk covered. Where a client's shop has attractive windows, then perhaps this suggests a certain business rationale in buying additional insurance cover.

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NEWS IN SORAINEN

■ Recent deals

Complex cross border merger of IF P&C Insurance operations

Sorainen is advising IF P&C Insurance in the process of reorganising its Baltic operations. Advice involves complex regulatory and corporate law issues related to the cross border merger of IF P&C Insurance companies in the Baltics. Project was led by partners Dr Tomas Kontautas, Eva Berlaus-Gulbe, Karin Madisson and senior associates Algirdas Peksys, Risto Agur.

Advising a leading insurer on a professional group civil liability insurance policy

Riga office has advised a leading insurer of specialty risks in Europe that underwrites insurance policies in fourteen countries across Europe, on a professional group civil liability insurance policy concluded with the managing body of a regulated profession in Latvia. Riga team was led by partners Eva Berlaus-Gulbe, Girts Ruda and associate Santa Selga.

Advising a leading real estate developer on professional civil liability regulation

Riga office has advised a leading real estate developer in Latvia on professional civil liability regulation of architects and possibilities to limit the developer's risk due to default by an architect. The Sorainen team in the project was represented by partner Girts Ruda, senior associate Lelde Lavina and associate Santa Selga.

Advising MAI Lietuva in acquisition of Draudimo efektas

Vilnius office has advised MAI Lietuva, part of MAI Central Eastern Europe, the largest independent network of insurance and reinsurance brokers within CEE, in acquisition of 100% shares in the insurance brokerage company Draudimo efektas, based in Kaunas. With this transaction, MAI Lietuva has expanded its activities in Lithuania and in addition to its office in Vilnius will also have an office in Kaunas, Lithuania's second biggest city. The Sorainen team for this case was led by partner Dr Tomas Kontautas and senior associate Raminta Karlonaitė.

■ Employees

New member of Insurance Team at Vilnius office

On 20 October 2008 Dr Tomas Talutis joined the Insurance Team at Vilnius office.

Tomas Talutis holds two master's degrees: a Master in Law from Vilnius University, and a LLM degree from Johann Wolfgang Goethe-University, Frankfurt. In 2008, he obtained the degree of Doctor (Dr) of Social Sciences (Law).

He has gained professional experience as a chief specialist with the Lithuanian Insurance Supervisory Commission where he worked for five years, and as a Commissioner (Member of the Board) at the Lithuanian Securities Commission for two years, where he was in charge of legal issues and implementation of the Markets in Financial Instruments Directive (MIFID).

Tomas Talutis is also a lecturer in Insurance Law at Mykolas Romeris University. By the end of 2009 Tomas Talutis will publish his first book on Insurance Intermediaries.

■ Other

Sorainen — the most awarded and internationally recognised regional law firm in the Baltics

During recent months, Sorainen has been recognised by several international publications. In December, *The Financial Times* and *Mergermarket* awarded Sorainen the title of the Best Legal Adviser in the Baltics. The awards ceremony was held in London, and its host, BBC business news presenter Declan Curry, said that the award went to the leading Baltic law firm, which advised on the largest number of transactions and for the largest total value in the Baltics.

Not long after that, in January, Sorainen received the Baltic Law Firm of the Year award from the international *PLC Which Lawyer?* Law Firm Awards 2009. The awards organizers explained that Sorainen was commended in particular for having “good people in all three countries” and for being “well-organised, timely and reasonable”.

In March, Sorainen was acknowledged as the Baltic Law Firm of the Year 2009 by the world's leading publication in the field of international finance – *International Financial Law Review* (IFLR). IFLR has been the world's leading magazine for more than 20 years for in-house counsel and practitioners in the financial markets.

Further information about the awards is available on our web site www.sorainen.com

