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Global Legal Group

# The International Comparative Legal Guide to: Securitisation 2011

A practical cross-border insight  
into securitisation work

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# Estonia



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## 1 Receivables Contracts

**1.1 Formalities. In order to create an enforceable debt obligation of the obligor to the seller, (a) is it necessary that the sales of goods or services are evidenced by a formal receivables contract; (b) are invoices alone sufficient; and (c) can a receivable “contract” be deemed to exist as a result of behaviour of the parties?**

- (a) There are no formal contract requirements applicable for the sale of goods (unless the sale involves securities) or services. The exceptions to this rule concern the relationship between a credit institution and its clients, any assumption of debt and sale of certain types of assets (e.g. real estate);
- (b) an invoice may be considered evidence for the conclusion of an oral contract, but it is at the discretion of the court in case of argument; and
- (c) if oral contracts are acceptable, an acceptance to enter into a contract may be presented by behaviour or the historic relationship of the parties may be deemed acceptable as a basis for the contract, for example if the parties have been involved in long-term commercial relations and one of them submits an offer for the conclusion of the contract, and the other party fails to timely object.

**1.2 Consumer Protections. Do Estonian laws (a) limit rates of interest on consumer credit, loans or other kinds of receivables; (b) provide a statutory right to interest on late payments; (c) permit consumers to cancel receivables for a specified period of time; or (d) provide other noteworthy rights to consumers with respect to receivables owing by them?**

- (a) The annual percentage rate payable by a consumer in connection with consumer loans is limited in Estonia. The respective rate may not exceed the average annual percentage rate of consumer loans granted in Estonia (published and calculated by the Central Bank) more than three times;
- (b) the late payment interest rate applicable regarding a consumer loan may not exceed the interest rate set forth in respective consumer loan contract. In the event parties have not agreed on the late payment interest rate, the late payment interest shall be the rate applicable to main refinancing operations of the European Central Bank plus 7 per cent per year. In case a contract prescribes the interest rate exceeding the late payment interest rate applicable under the law (see above), the interest rate stipulated in the contract shall serve as the basis for the late payment interest rate as well;

- (c) current laws do not permit consumers to cancel receivables for a specified period of time; and
- (d) a consumer has the right to early payment i.e., a consumer may perform his obligations arising from a consumer credit contract before due date and in such case the consumer does not owe interest or other charges for the period when the credit is not used.

Specific restrictions and consumer favourable regulation pertains to consumer protection regarding “doorstep” and distance agreements.

**1.3 Government Receivables. Where the receivables contract has been entered into with the government or a government agency, are there different requirements and laws that apply to the sale or collection of those receivables?**

No there are not.

## 2 Choice of Law - Receivables Contracts

**2.1 No Law Specified. If the seller and the obligor do not specify a choice of law in their receivables contract, what are the main principles in Estonia that will determine the governing law of the contract?**

The contract will be governed by the law of the state the contract is most closely connected to. The contract is presumed to be most closely connected to the state of residence or seat of the managing body of the party who is to perform the obligation characteristic of the contract at the time of entry into the contract.

If the contract is entered into in the course of the economic or professional activity of the party who is to perform the obligation characteristic of the contract, the contract is presumed to be most closely connected with the state where the principal place of business of such party is located. If under the terms of the contract the obligation characteristic to the contract shall be performed in a place of business other than the principal place of business, the contract is presumed to be most closely connected with the state where such other place of business is situated.

If the object of the contract is a real right regarding immovable property or a right to use immovable property, the contract is presumed to be most closely connected with the state where the immovable property is located.

**2.2 Base Case.** If the seller and the obligor are both resident in Estonia, and the transactions giving rise to the receivables and the payment of the receivables take place in Estonia, and the seller and the obligor choose the law of Estonia to govern the receivables contract, is there any reason why a court in Estonia would not give effect to their choice of law?

No there is not.

**2.3 Freedom to Choose Foreign Law of Non-Resident Seller or Obligor.** If the seller is resident in Estonia but the obligor is not, or if the obligor is resident in Estonia but the seller is not, and the seller and the obligor choose the foreign law of the obligor/seller to govern their receivables contract, will a court in Estonia give effect to the choice of foreign law? Are there any limitations to the recognition of foreign law (such as public policy or mandatory principles of law) that would typically apply in commercial relationships such that between the seller and the obligor under the receivables contract?

The parties to a contract are generally free to choose the applicable law. The choice of law of a foreign state is not applied if the result of such application would be in obvious conflict with the essential principles of Estonian law (public policy). In such case, Estonian law applies. In case a court in Estonia is unable to identify the content of a foreign law within a reasonable time despite all efforts, Estonian law applies. Furthermore, if the parties have chosen a foreign law to govern the contract, mandatory provisions of Estonian law are still applicable.

**2.4 CISG.** Is the United Nations Convention on the International Sale of Goods in effect in Estonia?

Yes, CISG is in effect in Estonia.

### 3 Choice of Law - Receivables Purchase Agreement

**3.1 Base Case.** Does Estonian law generally require the sale of receivables to be governed by the same law as the law governing the receivables themselves? If so, does that general rule apply irrespective of which law governs the receivables (i.e., Estonia's laws or foreign laws)? Are there any exceptions to this rule that would apply to receivables sale transactions?

Sale of receivables does not need to be governed under the same law as the receivables subject to such sale. However, regardless of the fact that the parties have chosen a foreign law to govern the contract, mandatory provisions of Estonian law are applicable. For instance, if the receivable is a registered security governed by Estonian law, the transfer of title to ownership of such receivable shall be exclusively governed by Estonian law.

**3.2 Freedom to Choose Other Law.** If (a) the receivables are governed by one country's laws (whether Estonian laws or foreign laws), (b) the seller sells the receivables to a purchaser located in a third country, and (c) the seller and the purchaser choose the law of the purchaser's country to govern the receivables purchase agreement, will a court in Estonia give effect to their choice of foreign law? Are there any exceptions to this rule that would apply to receivables sale transactions?

If the parties have chosen a foreign law to govern the receivables sale contract, a court upholds choice of law, unless the receivable represents a registered security, in which case the law of country where the relevant registry is situated shall apply to the property and related rights. However, if a court is unable to ascertain content of a foreign law to be applied within reasonable time despite all efforts, Estonian law shall be applied.

The court may also refuse to uphold the choice of law, in case the debtor is a consumer and the choice of law will result in depriving the debtor of the protection granted to him by the law of his state of residence. The court refuses to uphold the choice of law, if such is in conflict with Estonian public policy.

**3.3 Freedom to Choose Home Country Law.** Conversely, if (a) another country's law governs the receivables (e.g., a foreign obligor's country), and (b) the seller and purchaser are resident in Estonia, will a court in Estonia permit the seller and purchaser to choose the law of Estonia to govern the receivables sale? Will a court in Estonia permit the seller and purchaser to choose the law of Estonia to govern the receivables sale if only one of the seller or the purchaser are resident in Estonia? Are there any exceptions to this rule that would apply to receivables sale transactions?

Yes, a court upholds the choice of Estonian law. However, if the receivable represents a registered security, the law of country where the relevant registry is situated shall apply to the property and related rights, including transfer of title to ownership.

**3.4 Recognition of Foreign Law Sales.** If (a) both the receivables contract and the receivables purchase agreement are governed by the same foreign law, and (b) the requirements for a true sale have been fully met under that foreign law, will a court in Estonia recognise that sale as being effective against the seller, the obligors and other third parties (such as creditors or insolvency administrators of the seller and the obligors) without the need to comply with Estonia's own sale requirements? Are there any exceptions to this rule?

Yes, in general, a court upholds such sale. Notwithstanding the said, if the seller is an Estonian company, the court shall have a right to reverse such sale in the course of insolvency proceedings (please see question 6.3 below).

If a receivable under a receivable contract is a registered security or a mortgage governed by Estonian law, the title to ownership is transferred under Estonian law.

## 4 Asset Sales

### 4.1 Sale Methods Generally. In Estonia what are the customary methods for a seller to sell receivables to a purchaser?

It is customary to execute a factoring contract or assignment of claim agreement to sell receivables to a purchaser.

### 4.2 Perfection Generally. What formalities are required generally for perfecting (i.e., making enforceable against other creditors of the seller) a sale of receivables? Are there any additional or other formalities required for the sale of receivables to be perfected against any subsequent good faith purchasers for value of the same receivables from the seller?

There are no specific requirements regarding perfection of the sale of receivables. The major risk in connection with the sale of receivables is related earlier transactions, not regarding the subsequent transactions. There is a risk that the receivable has already been sold, in which case the former arrangement shall prevail over the latter.

If the receivable represents a registered security, the sale is enforceable against other creditors of the seller following the purchaser has entered into the relevant register as the owner of a registered security.

### 4.3 Perfection for Promissory Notes, etc. What additional or different requirements for sale and perfection apply to sales of promissory notes, mortgage loans, consumer loans or marketable debt securities?

A promissory note can be transferred to another person by means of an endorsement, unless the drawer of the promissory note has expressly excluded the transferability. If the drawer has excluded the transferability, the promissory note may be transferred as a registered security. A right arising from a registered security shall be transferred pursuant to the provisions concerning the transfer of the corresponding right in writing, concurrently with the transfer of the security. An endorsement of the promissory note shall be unconditional. An endorsement for partial transfer of the rights and obligations stipulated in a promissory note is void.

Loan agreements are form-free, unless concluded by a credit institution. However, since mortgage establishment requires an agreement certified by the notary public, the mortgage can be transferred in a notarised form. Consumer loans are generally concluded in writing, particularly where the lender is a credit institution, and therefore the purchase contract is also to be executed in writing.

The transfer of marketable debt securities is regulated depending on whether the debt security is registered with the Estonian Central Registry of Securities. If registered, the securities are transferred electronically from one securities account to another by the registrar. The regulation of the sale of non-registered debt securities may vary depending on the type of security. Marketing securities of special purpose entity established for securitisation may be deemed as a public offer of securities. An offer of securities is not regarded as public if the securities are offered solely (i) to a professional investor, (ii) to not more than ninety-nine persons per European Economic Area Member State, other than professional investors, or, (iii) an offer of securities addressed to investors who acquire securities for a total consideration of at least 50,000 EUR

per investor, for each separate offer, or (iv) an offer of securities whose denomination per unit amounts to at least 50,000 EUR, or (v) an issue or offer of securities with a total consideration of less than 100,000 EUR in a period of 12 months.

There are no specific restrictions as to the perfection of the sale of consumer loans. However, it should be noted that an agreement precluding or restricting a consumer's right to plead defences arising from a contract against third parties to whom the obligee assigns any claims arising for the consumer from a consumer credit contract or which precludes or restricts a consumer's right to set-off are void.

### 4.4 Obligor Notification or Consent. Must the seller or the purchaser notify obligors of the sale of receivables in order for the sale to be effective against the obligors and/or creditors of the seller? Must the seller or the purchaser obtain the obligors' consent to the sale of receivables in order for the sale to be an effective sale against the obligors? Does the answer to this question vary if (a) the receivables contract does not prohibit assignment but does not expressly permit assignment; or (b) the receivables contract expressly prohibits assignment? Are there any limitations regarding the purchaser notifying the obligor of the sale of receivables even after the insolvency of the seller or the obligor?

Under Estonian law the seller may assign receivables contract in part or in full regardless of the consent of the obligor. The obligor may assign his obligations only if the seller consents with such transfer.

The notification of the obligor is not compulsory but highly recommended bearing in mind the interests of the purchaser. The obligor may perform his obligations to the seller inasmuch a valid assignment document has been presented to him. Although, the purchaser has the right to receive such performance of an obligation from the seller. In addition the obligor may withhold the performance of his obligation to the purchaser until presented with a valid assignment document. The notification prevents the obligor from performance of his obligation to the seller. In case of the obligor's insolvency, the purchaser should notify the obligor within two months as of declaration of the obligor's insolvency. Depending on the time of notifying the obligor of the assignment there may be limitations on set-off of the receivable.

In case the receivables contract expressly prohibits assignment of receivables, the assignment carried out without the consent of the obligor is still valid but the seller is liable to the obligor for damages caused by the assignment in breach of the receivables contract.

### 4.5 Restrictions on Assignment; Liability to Obligor. Are restrictions in receivables contracts prohibiting sale or assignment generally enforceable in Estonia? Are there exceptions to this rule (e.g., for contracts between commercial entities)? If Estonia recognises prohibitions on sale or assignment and the seller nevertheless sells receivables to the purchaser, will either the seller or the purchaser be liable to the obligor for breach of contract or on any other basis?

Restrictions in receivables contracts prohibiting sale or assignment are not enforceable in Estonia in a sense that the assignment remains valid. However, the seller who has breached the receivables contract will be liable to the obligor for the accruing damages. The purchaser will not be liable for such breach.

**4.6 Identification.** Must the sale document specifically identify each of the receivables to be sold? If so, what specific information is required (e.g., obligor name, invoice number, invoice date, payment date, etc.)? Do the receivables being sold have to share objective characteristics? Alternatively, if the seller sells *all* of its receivables to the purchaser, is this sufficient identification of receivables?

No specific information is required for the assignment of receivables save for the requirement that the receivable is sufficiently identifiable. Also, it is possible to assign future receivables and contingent receivables if they are sufficiently defined at the time of the sale. Therefore, the contract for the sale of receivables should contain all the information reasonably required to identify the receivable being transferred.

We are of the opinion that if the seller sells *all* of its receivables to the purchaser it may not be sufficient for identification of receivables.

**4.7 Respect for Intent of Parties; Economic Effects on Sale.** If the parties denominate their transaction as a sale and state their intent that it be a sale will this automatically be respected or will a court enquire into the economic characteristics of the transaction? If the latter, what economic characteristics of a sale, if any, might prevent the sale from being perfected? Among other things, to what extent may the seller retain (a) credit risk; (b) interest rate risk; and/or (c) control of collections of receivables without jeopardising perfection?

Interpreting of a transaction will be based on the actual intent of the parties and among other things the court will look into the economic characteristic of the transaction.

The parties are free to agree that the seller will retain certain risks or control over the collection of the receivable.

**4.8 Continuous Sales of Receivables.** Can the seller agree in an enforceable manner (at least prior to its insolvency) to continuous sales of receivables (i.e., sales of receivables as and when they arise)?

The law requires that the receivables to be sold should be sufficiently identifiable at the moment of their sale. If this condition is met then such an agreement is enforceable.

**4.9 Future Receivables.** Can the seller commit in an enforceable manner to sell receivables to the purchaser that come into existence after the date of the receivables purchase agreement (e.g., “future flow” securitisation)? In that regard, is there a distinction between receivables that arise prior to or after the seller’s insolvency?

The transfer of the conditional receivables or those emerging in the future is allowed, if such receivables are sufficiently identifiable at the time of such sale. If before declaration of bankruptcy the debtor has disposed his future claims, the disposition becomes void upon declaration of bankruptcy in respect of the claims which arise after the declaration of bankruptcy.

**4.10 Related Security.** Must any additional formalities be fulfilled in order for the related security to be transferred concurrently with the sale of receivables? If not all related security can be enforceably transferred, what methods are customarily adopted to provide the purchaser the benefits of such related security?

Collateral related to the receivables is deemed to be transferred to the purchaser upon assignment (sale) of the claim (receivable), save for mortgages and other collaterals that are not deemed related to receivables. Collaterals not related to receivables are subject to separate and independent assignment procedure. Upon transfer of a receivable secured by a mortgage or by a registered security over a moveable, the obligor shall provide assistance in registering the transfer of security to the purchaser. Furthermore, assignment of a mortgage must be carried out in notarised form and registered in the Real Title Book.

## 5 Security Issues

**5.1 Back-up Security.** Is it customary in Estonia to take a “back-up” security interest over the seller’s ownership interest in the receivables and the related security, in the event that the sale is deemed by a court not to have been perfected?

No, it is not customary practice.

**5.2 Seller Security.** If so, what are the formalities for the seller granting a security interest in receivables and related security under the laws of Estonia, and for such security interest to be perfected?

Please see question 5.1 above.

**5.3 Purchaser Security.** What are the formalities for the purchaser granting a security interest in receivables and related security under the laws of Estonia, and for such security interest to be perfected?

Agreements regarding establishing a pledge must be entered into in writing. In order to establish a pledge of a claim (in Estonia: *nõuete pant*) over receivables, the pledgor and the pledgee have to reach an agreement regarding establishing security of a receivable contract. Under law it is not required to notify the obligor under the receivable contract about establishing a pledge of a claim to receivables if the pledgor and the pledgee agree so, however it is recommended.

The purchaser may grant security interest over the mortgage. For such arrangement, the purchaser is obliged to conclude the respective agreement in notarised form and entry into the Real Title Book is necessary for establishing such security.

**5.4 Recognition.** If the purchaser grants a security interest in the receivables under the laws of the purchaser’s country or a third country, and that security interest is valid and perfected under the laws of that other country, will it be treated as valid and perfected in Estonia or must additional steps be taken in Estonia?

Under Estonian law security arrangement can only be established under the law governing the receivable.

**5.5 Additional Formalities. What additional or different requirements apply to security interests in or connected to promissory notes, mortgage loans, consumer loans or marketable debt securities?**

If an endorsement of a promissory note contains a written declaration implying a pledge (a pledge endorsement), the holder of the promissory note may exercise all rights arising from the note as the pledgee.

A real right contract entered into for the establishment of a mortgage shall be notarised. Mortgage is created once respective entry has been made in the Land Register. Making an entry in the Land Register to establish a mortgage requires notarised application by the owner of an immovable.

A pledge over registered securities is created upon entry of the pledge in the Estonian Central Register of Securities. The registrar makes a notation concerning pledged securities upon respective application by the pledgor. In the case of financial collateral, the registrar transfers the securities pledged on the basis of a financial collateral arrangement to the special securities account of the pledgor on the order of the account administrator of the pledgor.

The encumbrance of non-registered debt securities depends on the type of debt security.

**5.6 Trusts. Does Estonia recognise trusts? If not, is there a mechanism whereby collections received by the seller in respect of sold receivables can be held or be deemed to be held separate and apart from the seller's own assets until turned over to the purchaser?**

Estonian law does not recognise trusts.

However, if the seller acts as a collector for the purchaser under a services contract then according to law the claims and movables which a mandatary acquires when performing a mandate in the mandatary's name but on account of the mandator, and claims and movables which the mandator transfers to the mandatary for performance of the mandate are not included in the bankruptcy estate of the mandatary and they cannot be subject to a claim against the mandatary in an enforcement procedure.

**5.7 Bank Accounts. Does Estonia recognise escrow accounts? Can security be taken over a bank account located in Estonia? If so, what is the typical method? Would courts in Estonia recognise a foreign-law grant of security (for example, an English law debenture) taken over a bank account located in Estonia?**

Escrow account arrangements are recognised in Estonia. The typical method for establishing a security over a bank account located in Estonia is the pledge of claims (in Estonian: *nõuete pantimine*) against the bank deriving from the account agreement. A court in Estonia shall not recognise a foreign-law security arrangement over a bank account located in Estonia as the claim against the bank deriving from the account agreement is governed by Estonian law and thereof the security arrangement is exclusively subject to Estonian law.

**6 Insolvency Laws**

**6.1 Stay of Action. If, after a sale of receivables that is otherwise perfected, the seller becomes subject to an insolvency proceeding, will Estonia insolvency laws automatically prohibit the purchaser from collecting, transferring or otherwise exercising ownership rights over the purchased receivables ("automatic stay")? Does the insolvency official have the ability to stay collection and enforcement actions until he determines that the sale is perfected? Would the answer be different if the purchaser is deemed to only be a secured party rather than the owner of the receivables?**

Estonian law recognises an automatic stay regime only in connection with pending compulsory execution proceedings with respect to the debtor's property. In such case the court shall stay such execution proceedings following the insolvency official being appointed. Regarding the answers to the second and the third question please see question 6.2 below.

**6.2 Insolvency Official's Powers. If there is no automatic stay, under what circumstances, if any, does the insolvency official have the power to prohibit the purchaser's exercise of rights (by means of injunction, stay order or other action)?**

Upon appointment of the insolvency official, regardless of whether the purchaser is a secured party to whose favour obligations under the receivables are fulfilled or owner of the receivables, the court conducting the proceedings is entitled to apply all measures prescribed for securing an action, including the seizure of the debtor's property which is in the possession of another person, a prohibition on other persons from transferring property to the defendant or performing other obligations with regard to the defendant, which may include an obligation to transfer property to a bailiff or to pay money in a bank account prescribed by the court and another measure considered necessary by the court.

**6.3 Suspect Period (Clawback). Under what facts or circumstances could the insolvency official rescind or reverse transactions that took place during a "suspect" or "preference" period before the commencement of the insolvency proceeding? What are the lengths of the "suspect" or "preference" periods in Estonia for (a) transactions between unrelated parties and (b) transactions between related parties?**

Under Estonian legislation, the court shall reverse transactions the debtor has made or acts prior to bankruptcy proceedings with a view to damaging the creditor's interests. General grounds for rescinding of transactions are the following: (i) the transaction is made during the period from the appointment of insolvency official until declaration of bankruptcy; (ii) the transaction is made within one year before the appointment of insolvency official, in case the other party to the transaction knew or should have known that the transaction damages the interests of the creditors; (iii) the transaction is made before commencement of the term specified in subsection (ii) in case the transaction was made within three years before the appointment of insolvency official, if the debtor intentionally damaged the interests of the creditors with the transaction and the other party to the transaction knew or should have known that the debtor damaged the interests of the creditors; and (iv) within five years before the appointment of insolvency official, in case the debtor intentionally damaged the interests of the

creditors with the transaction and the other party to the transaction was a person related to the debtor who knew or should have known of the damaging effect of such transaction to the debtors. In case the transaction is made six months before the court has appointed an insolvency official, the other party to this transaction is presumed to have known that the debtor damaged the interests of the creditors with the transaction and the person related to the debtor is presumed to know that the debtor intentionally damaged the interests of the creditors with named transaction.

**6.4 Substantive Consolidation. Under what facts or circumstances, if any, could the insolvency official consolidate the assets and liabilities of the purchaser with those of the seller or its affiliates in the insolvency proceeding?**

Estonian legislation does not recognise substantive consolidation regime. Furthermore, there are no circumstances under which the assets and liabilities of the purchaser can be consolidated with those of the seller.

However, it is possible for the insolvency official to set off claims of the debtor against claims of creditors in the course of the insolvency proceedings. In the event that a creditor had a right to set off the claim against the claim of the debtor before the declaration of bankruptcy, the creditor may set off the defended claim (claim recognised at the creditors' meeting) also after the declaration of bankruptcy. A petition for setting off a claim may be submitted until the last distribution proposal is submitted to the court. A claim acquired through assignment may be set off in bankruptcy proceedings only if the claim was assigned and the debtor was notified of the assignment in writing not later than three months before the declaration of bankruptcy. A claim against the debtor which is acquired through assignment shall not be set off if the claim was assigned within the preceding three years before the appointment of insolvency official and the debtor was insolvent at the time of the assignment and the person who acquired the claim was or should have been aware of the insolvency at the time of the assignment.

**6.5 Effect of Proceedings on Future Receivables. What is the effect of the initiation of insolvency proceedings on (a) sales of receivables that have not yet occurred or (b) on sales of receivables that have not yet come into existence?**

Any future sales of receivables may be hindered because the court will usually impose the prohibition on further disposal of the debtor's assets, and any transactions entered into by the debtor during the period from the appointment of insolvency official until declaration of bankruptcy are subject to reverse (clawback).

## 7 Special Rules

**7.1 Securitisation Law. Is there a special securitisation law (and/or special provisions in other laws) in Estonia establishing a legal framework for securitisation transactions? If so, what are the basics?**

There are no laws specifically providing for securitisation transactions.

**7.2 Securitisation Entities. Does Estonia have laws specifically providing for establishment of special purpose entities for securitisation? If so, what does the law provide as to: (a) requirements for establishment and management of such an entity; (b) legal attributes and benefits of the entity; and (c) any specific requirements as to the status of directors or shareholders?**

There are no laws specifically providing for the establishment of special purpose entities for securitisation.

**7.3 Non-Recourse Clause. Will a court in Estonia give effect to a contractual provision (even if the contract's governing law is the law of another country) limiting the recourse of parties to available funds?**

There are no legal grounds for invalidity of such provision.

**7.4 Non-Petition Clause. Will a court in Estonia give effect to a contractual provision (even if the contract's governing law is the law of another country) prohibiting the parties from: (a) taking legal action against the purchaser or another person; or (b) commencing an insolvency proceeding against the purchaser or another person?**

Generally, agreements under which liability is precluded or restricted for intentional acts are prohibited, and terms that are detrimental to the interests of a consumer are void. Under the Constitution of the Republic of Estonia, any person whose rights and freedoms are violated has a right of recourse to the courts. Therefore, the validity of agreement restricting the right to file for bankruptcy or other lawsuits is highly questionable. However, it is possible to waive claims against the purchaser and in such case, even if legal action is taken, the respective claim should remain unsatisfied.

**7.5 Independent Director. Will a court in Estonia give effect to a contractual provision (even if the contract's governing law is the law of another country) or a provision in a party's organisational documents prohibiting the directors from taking specified actions (including commencing an insolvency proceeding) without the affirmative vote of an independent director?**

In case the independent director is a member of the management board of an Estonian company and the company can only be represented by other members of the management board jointly with the independent director (provided such requirement is also registered in the Commercial Register) then transactions made without the participation of the independent director are null and void.

In case the independent director is a member of the supervisory board of an Estonian company and the management board acts without the consent of the supervisory board then the transactions made by the management board are still valid.

The prohibition on commencement of insolvency proceedings will not, however, have any practical implementation in regard to Estonian companies because the Estonian Commercial Code obliges members of the management board of the entity to initiate bankruptcy proceedings within 20 days of the appearance of permanent insolvency of the entity. Each member of the management board is entitled to submit bankruptcy petition irrespective of any provisions for joint representation rights. The breach of this duty will result in the personal civil and criminal liability of the member of the management board.

## 8 Regulatory Issues

**8.1 Required Authorisations, etc.** Assuming that the purchaser does no other business in Estonia, will its purchase and ownership or its collection and enforcement of receivables result in its being required to qualify to do business or to obtain any licence or its being subject to regulation as a financial institution in Estonia? Does the answer to the preceding question change if the purchaser does business with other sellers in Estonia?

No. Regarding permanent establishment in terms of taxation, please see question 9.6 below.

**8.2 Servicing.** Does the seller require any licences, etc., in order to continue to enforce and collect receivables following their sale to the purchaser, including to appear before a court? Does a third party replacement servicer require any licences, etc., in order to enforce and collect sold receivables?

No. However, certain legal profession requirements apply to a particular person appearing before a court.

**8.3 Data Protection.** Does Estonia have laws restricting the use or dissemination of data about or provided by obligors? If so, do these laws apply only to consumer obligors or also to enterprises?

There are a few restrictions on the use and dissemination of data about or provided by debtors. First, the Personal Data Protection Act prohibits consumer obligors and enterprises to process personal data about, or provided by a natural person without their prior consent. Second, the Credit Institutions Act imposes upon a credit institution an obligation to maintain banking secrecy. This obligation covers data about each client of the credit institution, including the obligors and enterprises. Such data may only be transmitted to any third person with the prior written consent of the client. Similar restrictions may apply to other institutions, such as insurance companies.

**8.4 Consumer Protection.** If the obligors are consumers, will the purchaser (including a bank acting as purchaser) be required to comply with any consumer protection law of Estonia? Briefly, what is required?

Generally, consumer protection acts apply with respect to the relationship between seller and consumer. We have assumed that the purchaser overtakes and the seller assigns the claim against the consumer based on the conditions stipulated in the receivable contract. Therefore, the legal position of the consumer will not change as the purchaser undertakes to comply with regulation deriving from the receivable contract and under the consumer protection regulation as one party to the contract is the consumer. However, the consumer protection rules are the same for purchaser as they are for the seller.

**8.5 Currency Restrictions.** Does Estonia have laws restricting the exchange of Estonian's currency for other currencies or the making of payments in Estonian's currency to persons outside the country?

Legal tender in Estonia is the Euro. There are no restrictions regarding the exchange of euro or the making payments in Euro to persons outside Estonia.

## 9 Taxation

**9.1 Withholding Taxes.** Will any part of payments on receivables by the obligors to the seller or the purchaser be subject to withholding taxes in Estonia? Does the answer depend on the nature of the receivables, whether they bear interest, their term to maturity, or where the seller or the purchaser is located?

Estonia has applied a corporate income tax system that shifts the point of taxation from the moment of earning the profits to the moment of their distribution. Corporate income tax is charged on profit distributions and implicit distributions (such as fringe benefits, gifts and donations, transfer pricing adjustments and expenditures not related to the business activities of the company). All of the above distributions are taxed at the rate of 21/79 of the net amount of distribution, which amounts to 21 per cent of the gross amount distributed. Undistributed profits are not subject to corporate income tax regardless of whether they are invested or retained.

In some cases the payments on receivables by the obligors to the seller or the purchaser can be subject to withholding taxes in Estonia, depending also on the nature of the receivable or where the seller or the purchaser is located.

Income tax must be withheld on interest income of non-residents that is significantly exceeding the amount of interest payable on similar debt obligations under the market conditions. Income tax must also be withheld on rental (or similar) income of real estate located in Estonia and other property subject to entry in an Estonian register. Royalty payments to non-residents and on income of non-residents derived from rendering services in Estonia are also subject to withholding tax. If the non-resident is a legal person located in a low tax rate territory, income tax is charged on all income derived from rendering services to Estonian residents, irrespective of where the services were rendered or used.

Non-residents located in countries Estonia has a tax treaty with may enjoy more favourable tax treatment than the withholding requirements described above.

**9.2 Seller Tax Accounting.** Does Estonia require that a specific accounting policy is adopted for tax purposes by the seller or purchaser in the context of a securitisation?

There is no special regulation or any specific accounting policy for tax purposes by the seller or purchaser in the context of a securitisation.

**9.3 Stamp Duty, etc.** Does Estonia impose stamp duty or other documentary taxes on sales of receivables?

Stamp duty is not chargeable on a sale of receivables. However, notary's fees may be relevant if sale of receivables or establishing/transferring collateral (e.g., mortgage) is carried out in the presence of notary public and stamp duties will be relevant if transferring mortgages registered in the Real Title Book.

**9.4 Value Added Taxes.** Does Estonia impose value added tax, sales tax or other similar taxes on sales of goods or services, on sales of receivables or on fees for collection agent services?

Estonia imposes value added tax ("VAT") on sales of goods and services. Obligation to register as a taxable person for value added tax purposes arises if the taxable turnover exceeds EUR 16,000 in a

calendar year. If receivables are sold through economic activity, VAT may be imposed in certain cases. For instance, an assignment of the receivable is considered to be subject to VAT if the consideration paid or received for the receivable differs from the nominal value of the receivable at the time of the transfer. A recent Supreme Court judgment considers this to be a debt collection service which is a taxable event for VAT purposes. At the same time the receivable itself transferred from one person to another during assignment of a claim or transfer of a debt is not a taxable supply as to an amount which equals the value of the receivable since a monetary claim is not a separately consumable benefit chargeable to VAT.

Regarding factoring service the taxable value of a factoring service is the contract fee and the fee for handling the accounts. If such amounts cannot be easily identified for the purposes of VAT-chargeable supply, the tax authorities can make an assessment and usually the difference of nominal value and the consideration paid for the receivable is treated as taxable supply of services. The receivable itself is not subject to taxation, but the contract fee and the fee for handling the accounts shall be taxable to the Estonian VAT of 20%.

In conclusion, there is no clear practice regarding taxation regarding sales of receivables, therefore the question of taxation should be carefully examined in each individual case.

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**9.5 Purchaser Liability. If the seller is required to pay value added tax, stamp duty or other taxes upon the sale of receivables (or on the sale of goods or services that give rise to the receivables) and the seller does not pay, then will the taxing authority be able to make claims for the unpaid tax against the purchaser or against the sold receivables or collections?**

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According to the VAT Act, the person liable for VAT is the person who creates the taxable supply as a result of the business. Thus, if the seller does not pay the tax, the claims for unpaid tax can only be made against the seller and not the purchaser or on the receivables or collections. It is the purchaser's obligation to identify whether the seller is registered as a VAT-liable person if the purchaser

deducts the input VAT amount from its VAT supply. In case of assignment of claims or transfer of debts, the purchaser may be deemed to have a VAT-chargeable supply with respect to the difference of the nominal value and the actual consideration paid for the transfer of debt or the assignment of claim. If the taxable supply and the obligation to pay VAT lies with the seller, the tax authorities do not usually have sufficient grounds to place their VAT claim against the purchaser.

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**9.6 Doing Business. Assuming that the purchaser conducts no other business in Estonia, would the purchaser's purchase of the receivables, its appointment of the seller as its servicer and collection agent, or its enforcement of the receivables against the obligors, make it liable to tax in Estonia?**

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The mere fact of the purchaser's purchase of the receivables does not make the purchaser liable to tax in Estonia. However, one should consider the permanent establishment risk in relation to the actual place it may have in Estonia where it carries out its activities collecting debts (fixed place of business) or by way of having an authorised representative that carries out activities as a collection agent.

If the purchaser appoints the seller as its servicer and collection agent, the seller can be considered to be a representative of a non-resident. If a representative of a non-resident operates in Estonia and is authorised to carry out and repeatedly carries out transactions in the name of the non-resident, such non-resident is deemed to have a permanent establishment in Estonia with respect to those transactions. The profits of a permanent establishment are taxed in the same way as the income of resident legal persons. Obligations are reduced for subjects of countries with which Estonia has a double taxation treaty.

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