

**COMMERCIAL LAWS OF
ESTONIA
December 2012
AN ASSESSMENT BY THE EBRD**

Office of the General Counsel



European Bank
for Reconstruction and Development

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Basis of Assessment: This document draws on legal assessment work conducted by the Bank (see www.ebrd.com/law) and was last updated during the preparation of the 2012 EBRD Strategy for Estonia, reflecting the situation at that time. The assessment is also grounded on the experience of the Office of the General Counsel in working on legal reform and EBRD investment activities in Estonia and does not constitute legal advice. For further information please contact ltt@ebrd.com.

1. Overall Assessment

Estonia has an advanced set of commercial laws, when compared with other transition countries where the Bank operates. However, improvements are desirable on a number of specific issues, *e.g.*, the regime for taking security over movables.

In the recent EBRD assessment of PPP laws and their effectiveness Estonia was rated as being in “high compliance” with international best standards. Current practice has demonstrated that successful execution of PPP projects is possible in the framework of current legislation; however, clearer provisions would be needed in the law as regards the provision of security and government support. There is also a need for institutional strengthening, *e.g.*, the creation of a PPP Unit would be welcome.

The Estonian corporate governance framework is generally sound, however, not all recommendations of the Financial Supervisory Authority (FSA) seem to be implemented in practice and the FSA could play a more effective role in ensuring that Estonian listed companies comply with corporate governance requirements.

Estonia is in the process of transposing the relevant EU energy efficiency *acquis*. It is expected that the government will introduce changes to the current regulatory framework if the discussed draft law is adopted by the Parliament. Energy efficiency is promoted in nearly every field but additional policy and legal efforts need to be made in the industry, transport and building sector.

The latest EBRD insolvency assessment revealed that the Estonian insolvency law provisions are of a very high quality as regards the commencement of proceedings and dealing with creditors and adequate when dealing with the assets of the estate. On the other hand, the assessment found that there is room for improvement in the provisions regulating reorganisation proceedings.

The 2010 EBRD Public Procurement assessment found Estonian public procurement legislation to be in very high compliance with international standards, however some legislative gaps were found with procurement efficiency instruments.

The legal framework regulating capital markets is well developed and in compliance with EU legislation, however, there is a lack of legal framework providing for close-out netting and its enforceability.

The laws governing secured transactions in Estonia have established a fairly straightforward system but some further liberalisation is probably needed.

The Estonian market has been fully liberalised since January 2001 but a key challenge is the roll-out of next generation broadband networks with sufficient capacity to underpin the government’s (and the EU’s) information society and knowledge economy objectives

2. The Legal System

2.1 *Constitution and courts*

The constitutional system of Estonia is based on the 1992 Constitution, adopted by a referendum and amended in 2003 to reflect accession to the European Union. The Constitution vests legislative

power with the unicameral Parliament (Riigikogu). The 101 members of the Parliament are elected every four years by a citizens' vote on the basis of proportional representation.

The President is the head of the state, elected for a five-year term by the Parliament. In the event that Parliament fails to elect the President after three attempts, a special electoral body composed of 374 members is formed to elect the President. The President designates the candidate for Prime Minister and appoints the members of the Government. The candidate then has to select members of the Government and submit his programme to the Parliament. The Parliament has to make a decision regarding the candidate with the proposed cabinet. During the term of the Government, the Parliament can express a vote of no confidence in the Government, Prime Minister or any other member of the cabinet, which may result in the resignation of the Government or of a specific Minister. If no confidence is expressed in the Government or the Prime Minister, the President of the Republic may, upon proposal of the Government call extraordinary elections for the Parliament.

The court system of Estonia has three tiers: 1) county, city, and administrative courts; 2) circuit courts; and 3) the Supreme Court. County, city and administrative courts are courts of first instance. Circuit courts are appellate courts and review judgments of the courts of first instance. The Supreme Court is the highest state court and reviews judgments by lower courts within the cassation proceedings. The Supreme Court is also the court of constitutional review and has the power to invalidate any legislation that is in conflict with the Constitution.

The President nominates and Parliament confirms the Chief Justice of the Supreme Court. Supreme Court judges are nominated by the Chief Justice and their appointment is endorsed by Parliament. The Chief Justice also nominates the judges to all other courts who are then appointed by the President. Judges may only be removed from office by the decision of a court.

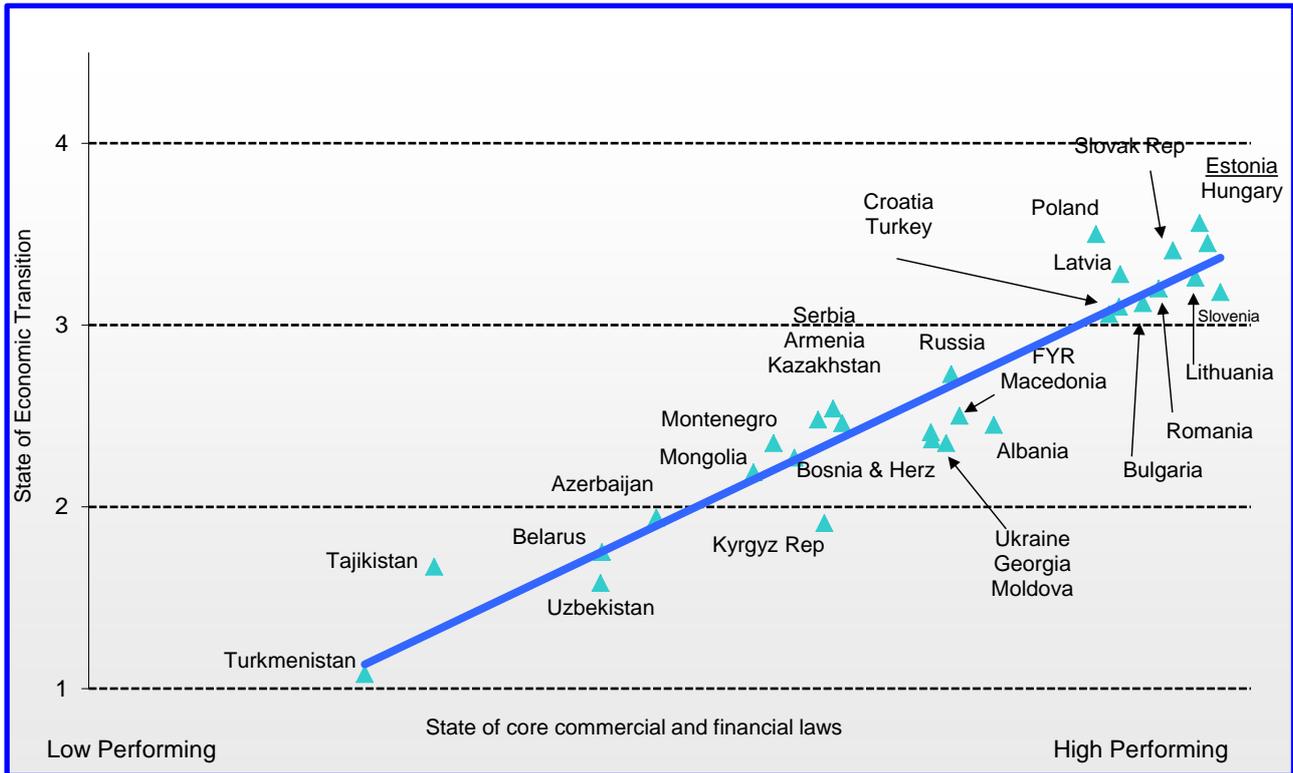
The Constitution also provides for the position of the Legal Chancellor who reviews the laws and regulations adopted by the legislative and executive powers and by local governments for conformity with the Constitution and other laws. In the event the issuing body does not comply with the recommendations of the Legal Chancellor, he/she will refer the document to the Supreme Court for invalidation.

2.2 Relationship between legal transition and economic progress

Since its independence, Estonia has made considerable progress in developing a stable and functioning market economy, and it is now considered one of the advanced transition countries in Central and Eastern Europe.

Moreover, the country has made significant progress in establishing the rule of law and democratic institutions. Experience in transition countries suggests that the degree of legal transition and economic development of the country advance or regress hand in hand, which is confirmed by data relating to Estonia

Chart 1 – Rule of law and progress in transition in the EBRD countries of operations



Source: EBRD Transition Report 2010 Table 1.1; EBRD Composite Country Law Index, July 2011

*Note: The **horizontal axis** measures the performance of commercial and financial laws. The **vertical axis** displays the EBRD transition index as an average of transition indicators between 1997 and 2011 with 1 referring to very early transition stages, and 4 referring to an advanced transition level.*

2.3 Recent developments in the investment climate

In the last couple of years Estonia has made significant progress towards developing a market economy. Accession to the European Union in 2004 reasserted Estonia's success in terms of legal and economic development. The government of Estonia is keen on attracting foreign direct investment and has been following policies supportive to and welcoming of foreign investment. Foreign and domestic companies are treated equally and Estonian law allows 100% foreign ownership of local companies.

Despite the fact that Estonia was severely impacted by the crisis, the economy has been on a solid recovery path. In fact, Estonia has recorded the strongest growth of any EU country in the first half of 2011. The World Bank's Doing Business Report 2012 ranked Estonia 24th out of 183 countries assessed. Furthermore, Transparency International's Corruption Perceptions Index ranked Estonia 29th out of 183 countries and in general, foreign investors do not see corruption as a serious issue in Estonia.

Adoption of the Euro in January 2011 has boosted investor and consumer confidence. Strong economic growth in 2011 is being boosted by an exceptional export performance in the technology-intensive sector. The fiscal consolidation programme following the financial crisis allowed for a better-than-expected deficit. In addition, gross public debt remains at the lowest level in the European Union.

2.4 Freedom of Information

Estonia is one of the countries in Eastern Europe with an especially effective freedom of information framework. The right to access information held by public authorities is declared as a constitutional right and defined by Article 44 of the Constitution. The Public Information Act (the Act) was passed by Parliament in November 2000 and entered into force on 1 January 2001.

The Act covers state and local agencies, legal persons and private entities that are conducting public duties. Any person may make a request for information and the holder of the information must respond within five working days. Requests for information are registered. Fees may be waived if information is requested for research purposes.

The Act also includes significant provisions on electronic access and disclosure. Government departments must maintain document registers. National and local government departments and other holders of public information must maintain websites and post an extensive list of information on the Web (*e.g.*, crime statistics, job descriptions of officials, their addresses, qualifications and salary rates, health and safety information, budgets and draft budgets, environmental information, draft acts and regulations etc.).

The Act is enforced by the Data Protection Inspectorate. The Inspectorate can review the procedures of the public authorities and receives complaints. Its officials can demand explanations from government bodies and examine their internal documents. The Inspectorate can order a body to comply with the Act and release documents. A review by the Council of Europe in 2004 found that the Act was successful in promoting access to information.

3. Evaluation of selected commercial laws

The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: concessions, corporate governance, energy, insolvency, judicial capacity, public procurement, secured transactions, securities markets and telecommunications. The existing tools assess both the quality of the laws “on the books” (also referred to as “extensiveness”) and the actual implementation of such laws (also referred to as “effectiveness”). This section presents a summary of the results accompanied by critical comments of the Bank’s legal experts who have conducted the assessments.

All available results of these assessments can be found at www.ebrd.com/law.

3.1 Concessions

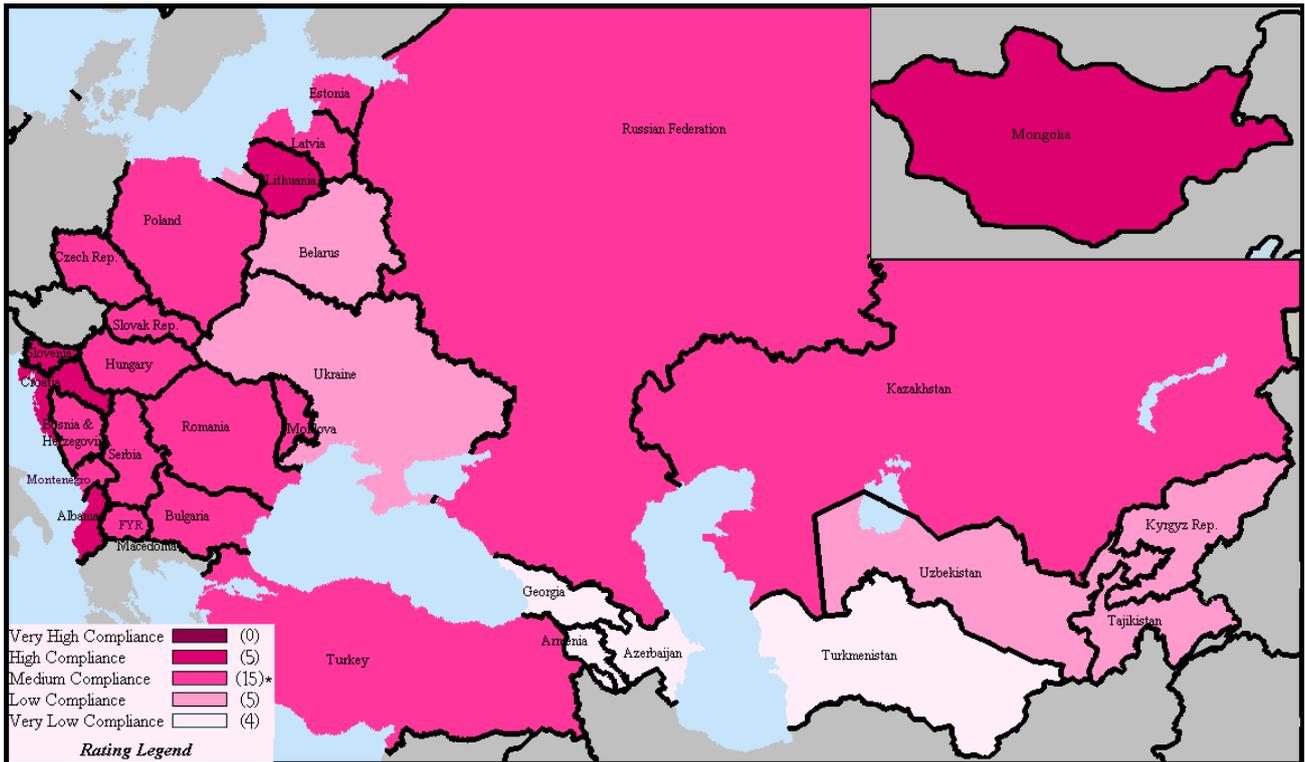
In Estonia there is no one single act dealing specifically with PPP projects or concessions. These are largely regulated by the Public Procurement Act. In addition, the Competition Act in conjunction with the Government’s Decree “Procedure for organising a public competition for the grant of special or exclusive rights” sets out the procedure for the organisation of public competitions for granting special or exclusive rights. Aside from the Guidelines on the Public Procurement Proceedings issued by the Ministry of Finance, no other PPP administrative guidance, framework or policy has been adopted.

However, it should be noted that the PPP/concession rules have gone through some noteworthy amendments and improvements. On 1 January 2011, the legislation containing the definition of PPPs and the conditions for the transfer of the rights and obligations deriving from a public procurement contract or a concession to a third person in PPP projects was incorporated into the Public Procurement Act. Further developments in the PPP sector are also illustrated by the fact that a number of PPP projects have already been initiated and implemented. Moreover, the adjudicative practice with regard to PPP projects is in the process of evolving, as some court decisions can already be distinguished clarifying the respective legal field in Estonia.

Practice has thus demonstrated that successful execution of PPP projects is possible in the framework of current legislation but more detailed PPP specific legislation and institutions (such as a PPP Unit) would be welcome as well as clearer provisions concerning security and government potential support (see Chart 3).

In the recent EBRD assessment of PPP laws and their effectiveness Estonia was rated in “low compliance” with international best standards (see Chart 2) and but “low effectiveness” for its practices.

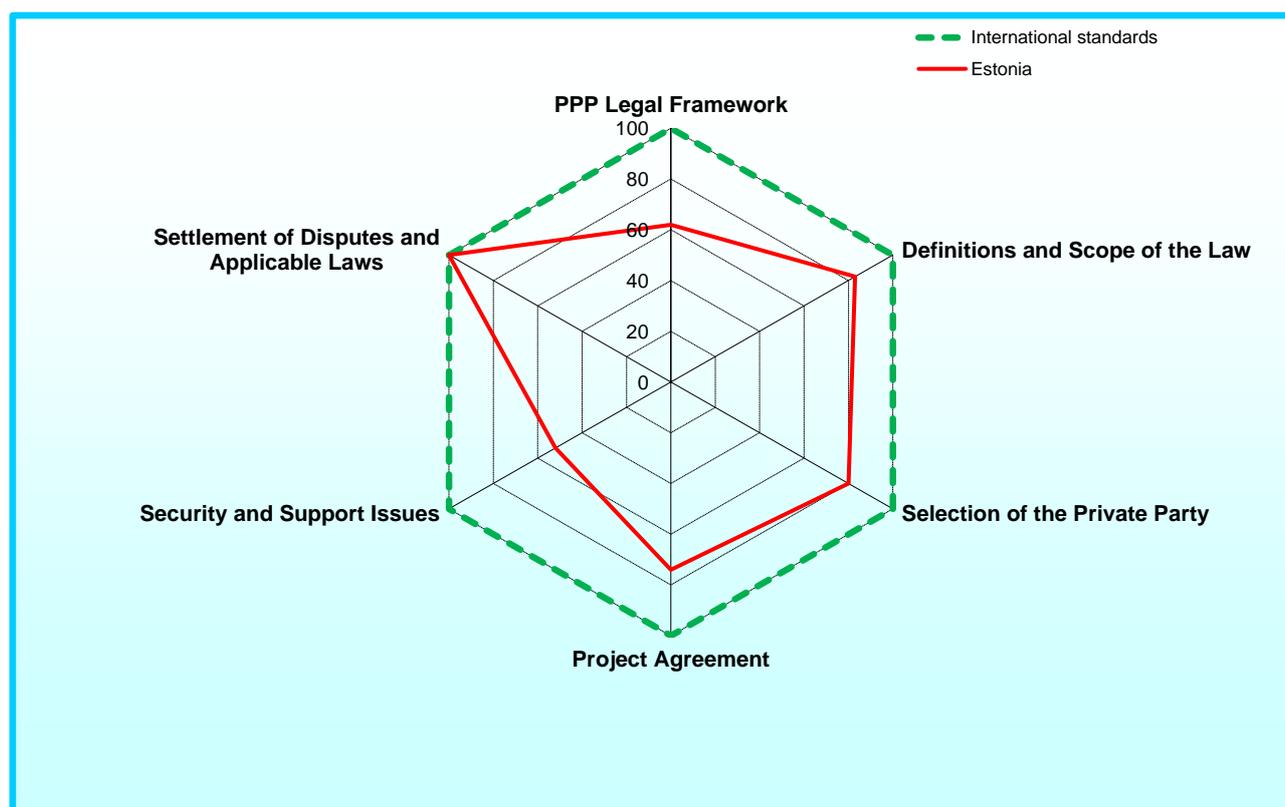
Chart 2 – Quality of concessions legislation in the EBRD countries of operations



Source: EBRD Concessions Sector Assessment 2011/12

Note: The various categories represent the level of compliance of a given country’s legislation (“the laws on the books”) with international standards such as the UNCITRAL Model Legislative Provisions on Privately Financed Infrastructure Projects. The asterisk indicates in which category Estonia ranks.

Chart 3 – Quality of concessions legislation – Estonia (2011/12)



Source: EBRD Concessions Sector Assessment 2011/12

Note: The extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the ‘web’, the more closely concessions laws of the country approximate these standards.

3.2 Corporate governance

The Commercial Code, entered into force in September 2005, as amended, is the primary legislation concerning corporate matters and governance in Estonia.

The Auditing Act was enacted on 27 January 2010 and entered into force on 8 March 2010. The Act introduces mandatory audit committees for companies over a certain size and for public interest companies. It also sets a mandatory requirement for rotation of auditors after 7 years.

In 2006, the Financial Supervisory Authority (FSA) in co-operation with the Tallinn Stock Exchange (TSE) adopted a set of voluntary “Corporate Governance Recommendations” intended to enhance corporate governance and transparency among listed companies. Pursuant to the TSE rules, listed companies are required to report their compliance with the Recommendations on a “comply or explain” basis.

Estonia’s legal framework has been amended several times in the last few years in order to harmonise the national legislation with the *Acquis Communautaire*. The corporate governance framework now appears to be of good overall quality. In the EBRD Corporate Governance Sector Assessment 2007 Estonia was scored as being in “medium compliance” with international best

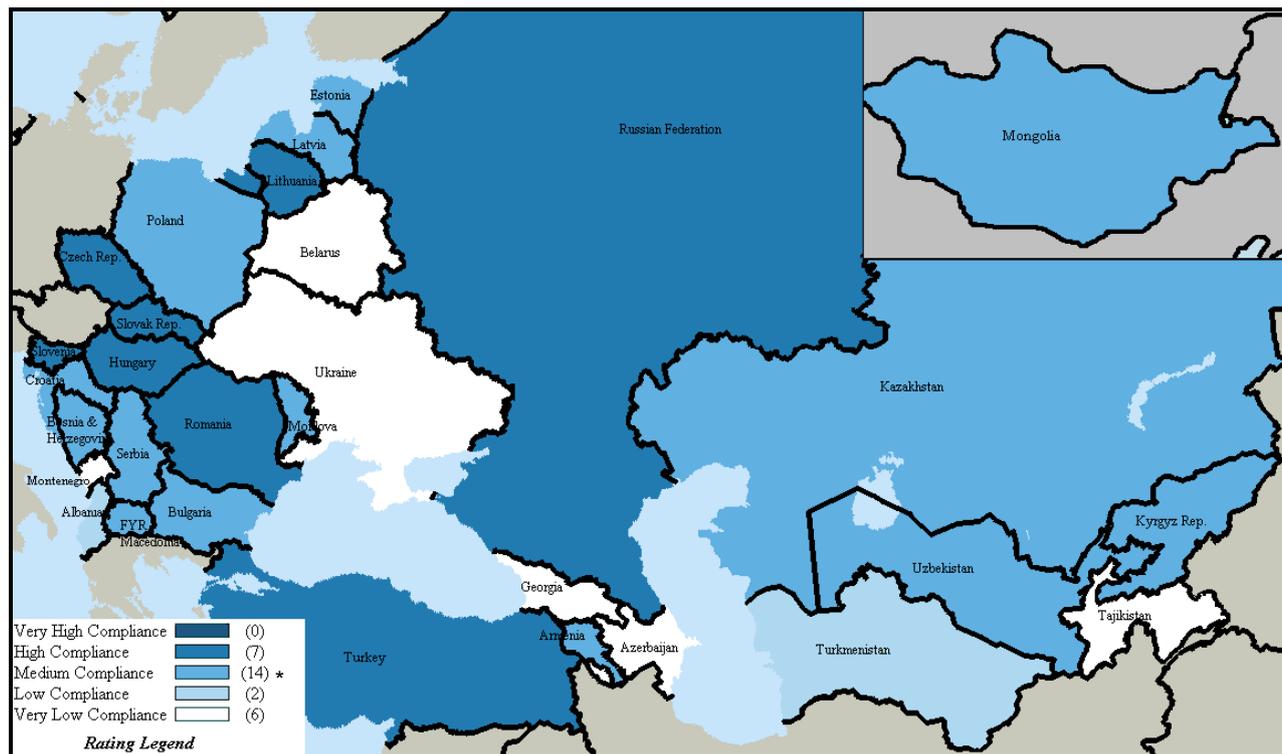
standards (see Chart 4). The market for listed companies is small (14 companies listed in 2011) and market mechanisms play a limited role in providing incentives for good corporate governance.

The FSA is seen as a competent and independent supervisor. The FSA also has an active role in revising the “comply or explain” statements presented by listed companies and in highlighting shortcomings in the reporting. Unfortunately, not all FSA recommendations seem to be implemented in practice and the FSA could play a more effective role in ensuring that Estonian listed companies comply with corporate governance requirements. Fines issued have been low and efforts to prosecute market abuse cases had only limited success. The cooperation between the FSA and the Public Prosecutor’s Office has improved but the sanctioning capacity of the FSA should be improved in order to deter non-compliance.

Reporting by listed companies on their compliance with the Corporate Governance Recommendations has room for improvement (see Chart 5): disclosure on board members’ qualifications and board composition should be clarified; strengthening the role of independent board members should also be considered, especially in relation to audit committees; the FSA could also play an effective role in ensuring that Estonian listed companies comply with corporate governance requirements.

The Estonian corporate governance framework is generally sound and the FSA is seen as a competent and independent regulator. The shortcomings highlighted in previous EBRD corporate governance assessments (especially relating to disclosure and transparency) have been addressed.

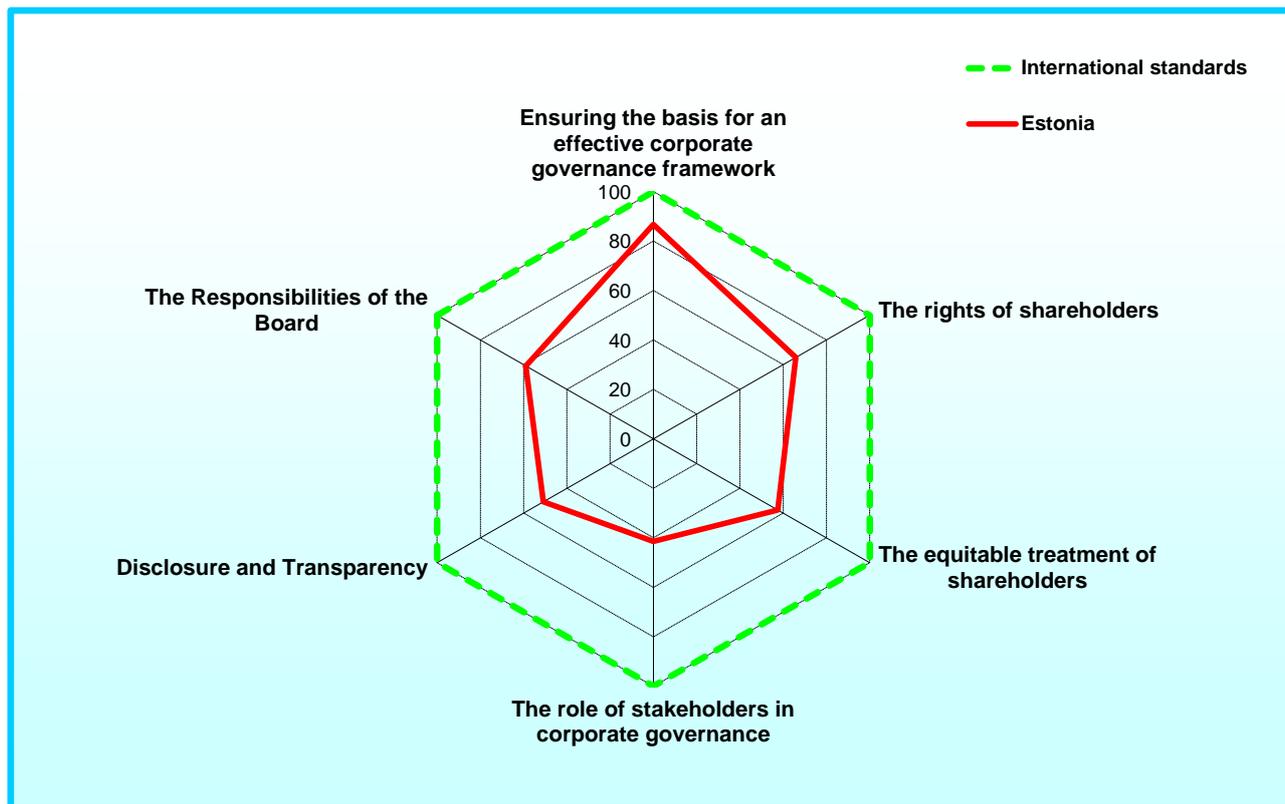
Chart 4 – Quality of corporate governance legislation in the EBRD countries of operations



Source: EBRD Corporate Governance Sector Assessment 2007

Note: The various categories represent the level of compliance of a country’s legislation (the “laws on the books”) with international standards as set out in the OECD Principles of Corporate Governance. The asterisk indicates in which category Estonia ranks.

Chart 5 – Quality of corporate governance legislation in Estonia (2007)



Source: EBRD Corporate Governance Sector Assessment 2007

Note: The extremity of each axis represents an ideal score, i.e., corresponding to OECD Principles of Corporate Governance. The fuller the ‘web’, the more closely the corporate governance laws of the country approximate these principles.

3.3 Energy

The main sector law regulating energy from renewable sources is the Electricity Market Act of 2003 (as amended).

The Estonian electricity market is characterised by an extreme concentration and reliance on oil shale. Essentially all generation is controlled by the largest energy enterprise Eesti Energia AS which possesses more than 90% of installed capacity. The recent EBRD assessment of energy laws and practices has shown that the market framework is the biggest gap in the country’s energy as compared to international best standards (see Charts 6 and 7). Only about 35% of the Estonian electricity market has been liberalised but a full market opening is planned to take place on 1 January 2013. At present, the Estonian Competition Authority regulates energy prices, which in practice applies only to prices to small consumers. All other electricity generators selling electricity to large customers (with a consumption capacity of over 2GWh) are free to fix their electricity prices and choose their own customers. The tariff structure has been identified by the recent EBRD assessment of energy laws and practices as one of the country’s strengths (see Charts 6 and 7).

Estonia’s Competition Authority estimates that renewable energy production in the country would reach more than 14% of final consumption of energy in 2012, while the country’s renewable energy target is 25% by 2020. After the adoption of the Electricity Market Act in 2003, the share of renewable energy increased mainly through growing production of wind energy and more recently, the use of wood and biomass. The feed-in-tariffs for renewable energy were revoked in February

2010. Renewable energy generators (except biomass) are paid a premium for the amount of EUR 53.70 / MWh for a fixed number of years (e.g., 12 years for wind energy). There are limits to the maximum amount of premiums paid depending on the type of renewable technology. Producers of wind power would receive less once total electricity produced from wind power exceeds the cap of 600 GWh (it is expected that this cap will be reached within the next couple of years).

In 2010 the Estonian government was contemplating retroactive cuts to premiums paid to renewable energy generators, which met with loud criticism from the international investors' community. After the parliamentary elections in April 2011, the government indicated that they were not planning to introduce cuts to the tariffs, which sent a sigh of relief across the sector. Nonetheless, at the end of 2011 the government again initiated talks about potential cuts to renewable energy premiums. On 31 January 2012, the Ministry of Economy published a new draft law providing for cuts to premiums up to 50%, depending on the type of renewables, envisioning also retroactive application of the draft law to existing plants.

The draft law has already been introduced for parliamentary review (and has passed two out of three parliamentary readings). Amidst protests by operators, in May 2012 the government has ensured investors that the revision of the premium levels for existing projects will not be applied unless an agreement to that effect has been reached with market participants.

With respect to diversification of energy sources, Estonia has to establish sufficient energy connections in the region, which would promote projects developed on the basis of local energy sources.

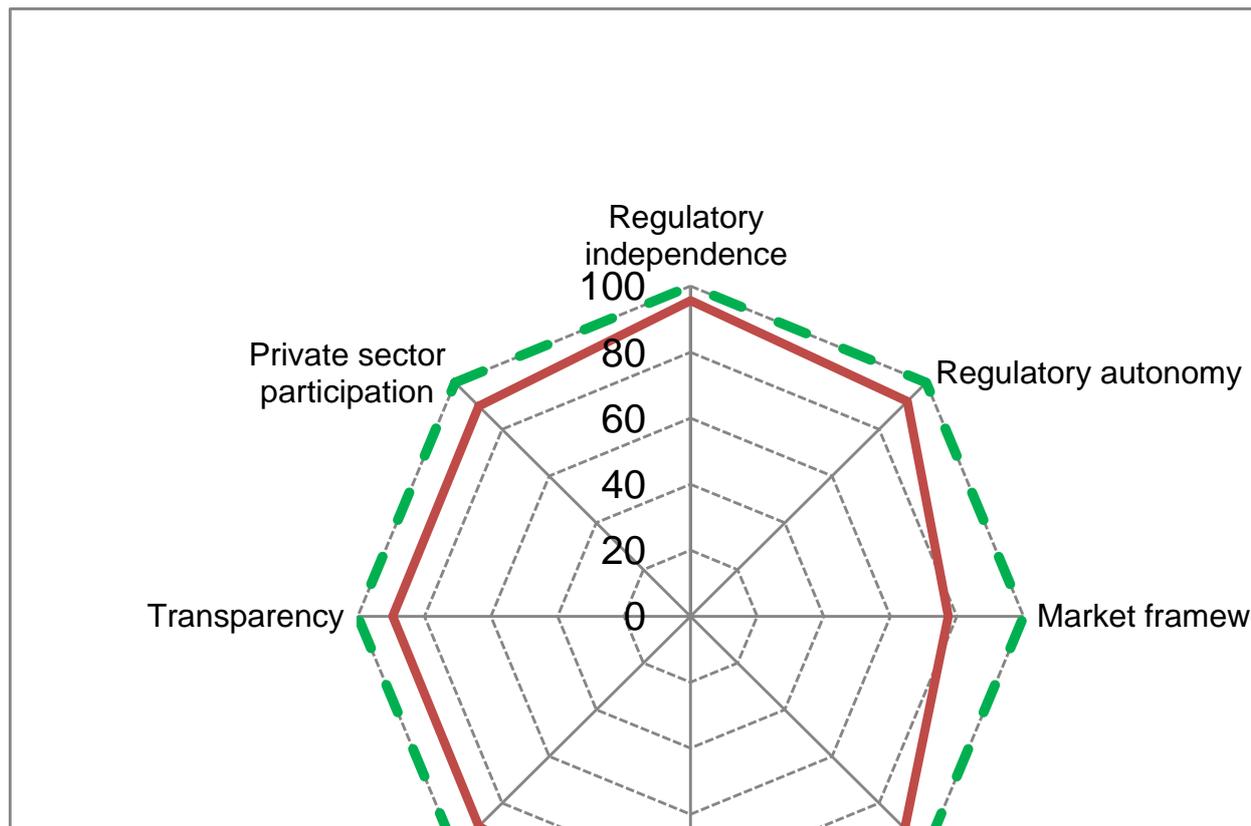
In light of better competitiveness as well as obligations undertaken to the European Union, one of the government's objectives is to maintain total energy consumption at the 2010 level. Estonia is in the process of transposing the relevant EU energy efficiency *acquis*, including the recast Directive 2010/31/EU on the energy performance of buildings.

The government has to ensure that all legal amendments to the existing regulatory framework for renewable energy enter into force only after an open and transparent consultation with stakeholders. The government has to guarantee legal certainty and predictability in the legal regime for the energy sector, including in relation to the planned revisions of the renewable energy premiums as well as the timeframe for reaching the 600GWh cap for wind generation.

Energy efficiency is promoted in nearly every field but additional policy and legal efforts need to be made in the industrial sector (especially power production), transport and buildings (both in the public and private sectors).

In order to keep its energy consumption at the 2010 level, Estonia's target for 2020, the government will have to focus on diversification of energy sources, increase in energy efficiency and promotion of the development of renewable energy.

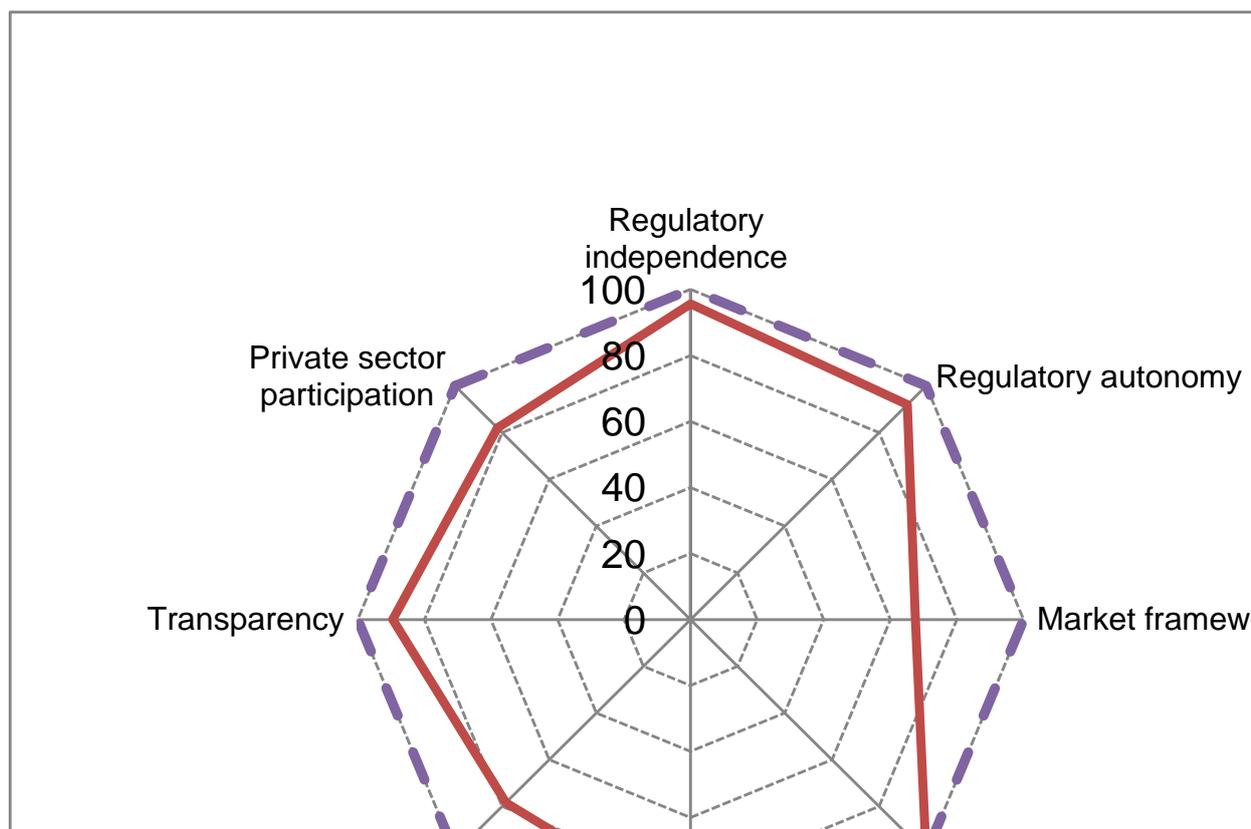
Chart 6 – Quality of energy (electricity) legislation in Estonia (2009)



Source: EBRD Energy law reform dimensions assessment project, 2009

Note: The extremity of each axis represents an ideal score, i.e., corresponding to the benchmarks and indicators identified in the assessment model. The fuller the 'web', the more closely the energy laws of the country approximate these principles.

Chart 7 – Quality of energy (gas) legislation in Estonia (2009)



Source: EBRD Energy law reform dimensions assessment project, 2009

Note: The extremity of each axis represents an ideal score, i.e., corresponding to the benchmarks and indicators identified in the assessment model. The fuller the ‘web’, the more closely the energy laws of the country approximate these principles.

3.4 Insolvency

Estonia’s legal framework in the insolvency sector is based on the Bankruptcy Act of 2003 (the “Bankruptcy Act”), which provides for (i) liquidation proceedings or, alternatively, (ii) reorganisation proceedings for insolvent debtors, and the Reorganisation Act of 2008 (the “Reorganisation Act”), which applies to debtors that are in financial difficulty and will probably become insolvent in the future.

The EBRD Insolvency Sector Assessment (the “Assessment”) completed in late 2009 rated Estonia as being in “high compliance” with international best standards (see Chart 8). Specifically, the Assessment concluded that the Estonian insolvency law provisions are of very high quality as regards commencement of proceedings and dealing with creditors and adequate as regards the assets of the estate. At the same time, the Assessment noted a potential for improvement in the law with respect to reorganisation proceedings, in particular relating to the information that must be disclosed to creditors, the ability to have an independent analysis of the plan and lack of any requirement that the plan must return to creditors an amount at least equal to what they would receive during the process of a liquidation; the Assessment further noted that there was no restriction on voting on reorganisation plans by connected parties in Estonia (see Chart 9).

Among its positive features, the Bankruptcy Act contains adequate provisions detailing the financial conditions that triggers insolvency and evidence required to establish such conditions, the process

for hearing and determining applications and the qualifications required for an insolvency administrator. In addition, the Bankruptcy Act contains particularly well-detailed provisions for the avoidance of pre-bankruptcy transactions.

The prior lack of a rehabilitation (reorganisation) process outside of bankruptcy, identified as a concern by the EBRD in the past, has been addressed with the adoption of the Reorganisation Act ('the Act'). The purpose of reorganisation under the Act is to overcome economic difficulties, restore liquidity, improve profitability and ensure sustainable management. Positive features of the Act include a stay on enforcement proceedings against the debtor's assets and the suspension of fines or other penalties for late payment, all of which provide the debtor with breathing space to develop a reorganisation proposal. During proceedings the business activities of the debtor are supervised by a reorganisation adviser, thus minimising the risk of abuse of process by the debtor. The lack of regulation governing the sale of assets under the Act (which in respect of bankruptcy is prescribed by the Bankruptcy Act) provides the debtor with flexibility to implement a reorganisation. The Act thus constitutes a big step towards improving the chances of survival of viable business entities while reducing the number of liquidations.

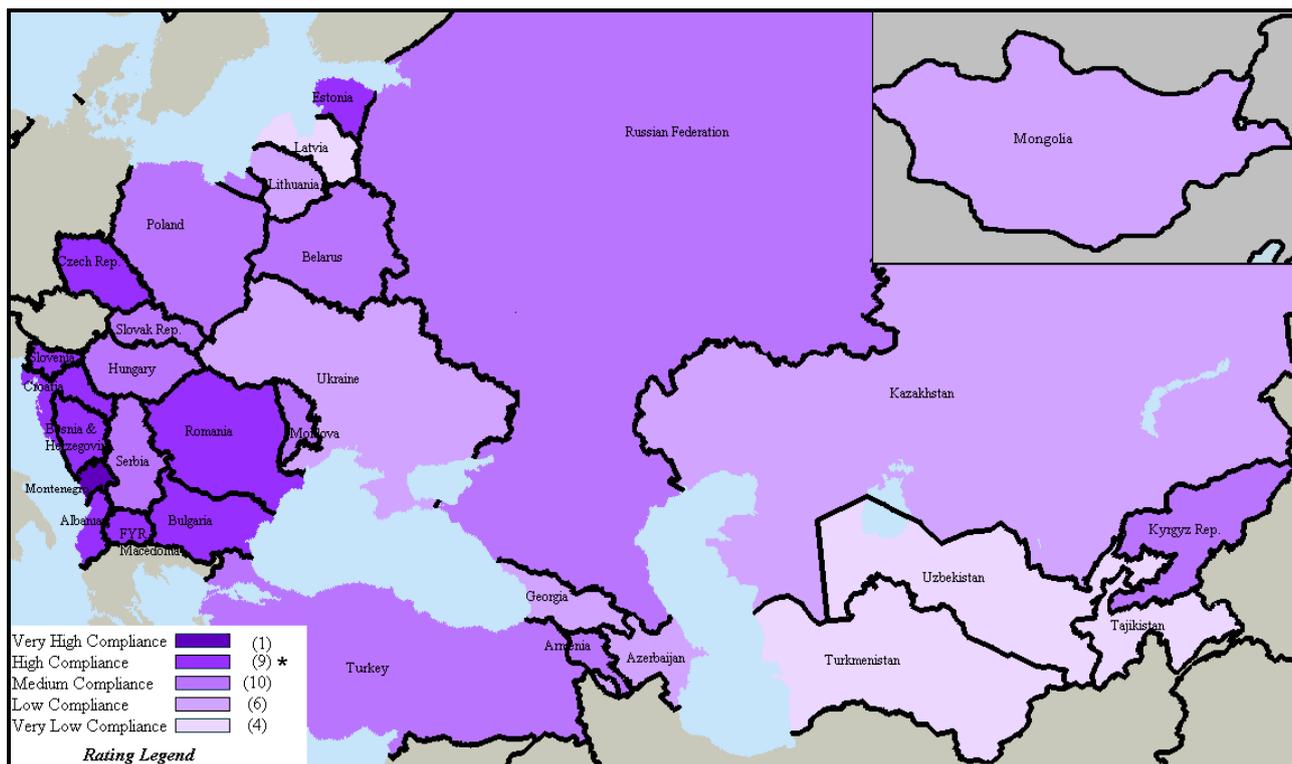
Negative features with respect to insolvency law generally include the absence of provisions under Estonian law requiring a third party in possession of assets of the estate of a debtor to deliver up such assets or make them available to the relevant functionary; this is in contrast to disclosure of information by third parties, which is required by law. In terms of secured creditors, creditors benefiting from security in the form of a pledge ("pledgees") are required to bear the costs of payments related to the bankruptcy proceedings, including costs arising from the recovery of assets and the proceedings themselves. Whilst this is subject to an overall cap of 15% of the money received from the sale of the pledged object (Section 153(2) of the Bankruptcy Act), as demonstrated by a recent Supreme Court ruling (Civil Case 3-2-1-167-11, February 20 2012), pledgees must be attentive and file an objection in due time to any breach of this legislative cap in order to protect their rights.

Since the EBRD Assessment there have been developments in the realm of personal insolvency: from April 2011 private individuals can be restructured in the same way as companies under court supervision. At present there is no pending draft legislation applicable only to bankruptcy and reorganisation. However insolvency proceedings are court-supervised and the legislature has adopted some changes to the Code of Civil Procedures in order to make proceedings more efficient.

The introduction of the Reorganisation Act in 2008 addressed a significant gap in Estonia's insolvency legal framework. The policy going forward should be to monitor the effectiveness of the Reorganisation Law and its accessibility by debtors in financial difficulty. Furthermore, consideration should be given to the protection of secured creditors in insolvency and minimisation insofar as possible of the proportion of secured assets available for satisfaction of the costs of bankruptcy proceedings under the Bankruptcy Law, as this may act as a disincentive to secured credit.

Estonia has the main tools of a modern insolvency law, providing both for liquidation and for reorganisation of the debtor's business (including reorganisation outside of bankruptcy).

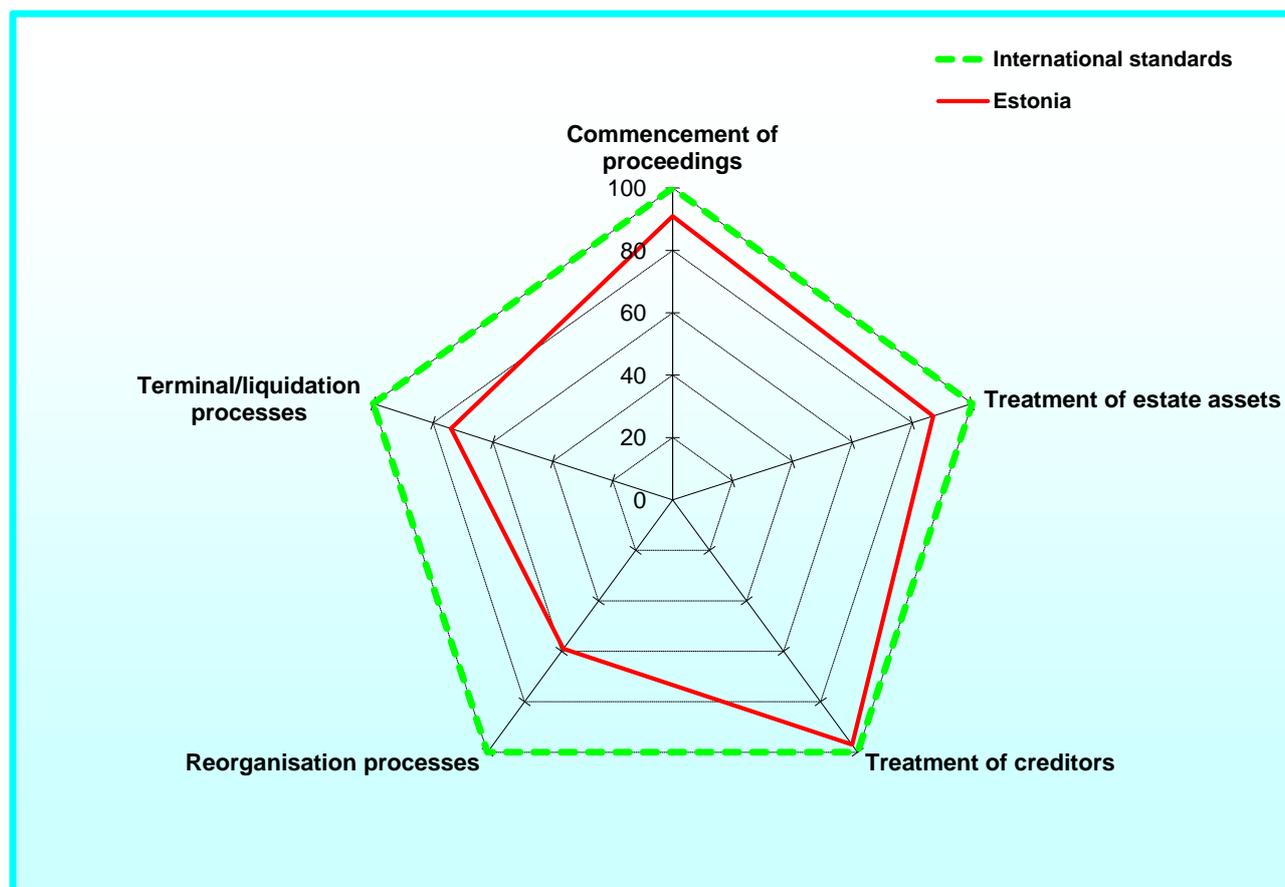
Chart 8 – Quality of insolvency legislation in the EBRD countries of operations



Source: EBRD Insolvency Sector Assessment 2009

Note: The various categories indicate the level of compliance of each country’s legislation (the “laws on the books”) with international standards, such as the World Bank’s Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on Legislative Guidelines for Insolvency Law, and others.

Chart 9 – Quality of insolvency legislation in Estonia (2009)



Source: EBRD Insolvency Sector Assessment 2009

Note: The extremity of each axis represents an ideal score, i.e., corresponding to international standards such as the World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group's "Legislative Guidelines for Insolvency Law", and others.

3.4 Judicial Capacity

Estonia is considered to have a well-functioning court system that deals efficiently with commercial matters.

Judges receive life tenure upon appointment to judicial office. Courts are well funded and resourced. The Supreme Court is allocated a dedicated percentage of the national budget. However, the financing of the lower courts is set by the Ministry of Justice, which has attracted some controversy as it potentially affects the independence of these courts.

Recent reforms have focused on court consolidation and management. The number of courts was reduced by merging the territorial jurisdictions of the existing courts. The previous 16 city and county courts were reduced to four, and the four administrative courts amalgamated into two. The objective of the changes was to improve the administration of justice, since larger courts make it more possible to evenly distribute the courts' work load among judges and reduce the time of judicial proceedings. Having fewer courts was also considered appropriate in the context of Estonia's small population size.

In addition, the adoption of a new Civil Procedure Code and Execution of Judgment Procedure Code has helped to speed up proceedings and reduce the number of disputes related to procedural law. The court system has embraced modern technology. An interesting feature introduced by new provisions is the ability to file actions electronically.

3.5 Public procurement

Public procurement in Estonia is regulated by the Public Procurement Act (the PPA), as amended. The latest amendment took place in 2011 and aimed to introduce electronic communication and e-auctions in the Estonian public procurement framework.

The PPA is based on transparency and competition principles in alignment with the EU public procurement directives and in the 2010 EBRD Public Procurement Assessment was rated within those areas as being in “very highly compliant” with international standards (90 per cent compliance rate) (see Chart 11).

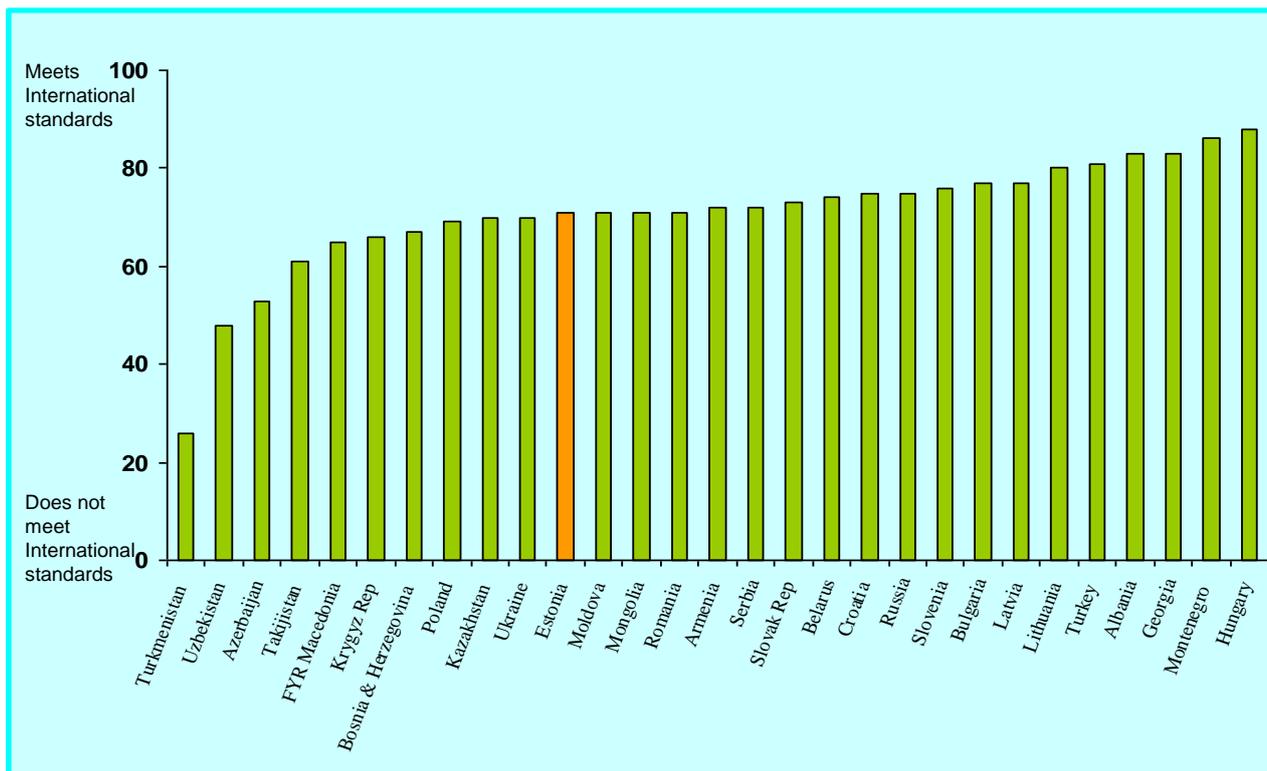
The PPA provides for procurement methods suitable for different contract types. Tenders, open and restricted, are the default procurement methods; the contracting entity may apply negotiated procedures only in situations where the law allows. The PPA establishes the requirement for mandatory electronic publication of advance procurement and contract notices as well as an obligation to publish the contract award notice for every public contract finalised by the contracting entity. The PPA also provides for a contemporary administrative enforcement mechanism and an independent remedies system.

The PPA further provides for modern and uniform regulation, in accordance with EU PP Directives; however, not all integrity safeguards and efficiency instruments recommended by international standards have been adopted in Estonia. Overall, the national public procurement policies in Estonia are focused on adopting integrity safeguards; the PPA is less comprehensive when it comes to procurement efficiency instruments and does not sufficiently regulate pre-tendering and post-tendering phases of the procurement process (see Chart 11).

Overall, in the 2010 EBRD Public Procurement Assessment, local public procurement practice in Estonia scored well and was reported to be in good compliance with international best practice (see Chart 10). However, some implementation problems were reported, related to internal allocation of roles in the procurement process and contract monitoring and auditing arrangements not always established by contracting entities (see Chart 11).

The public procurement legal framework in Estonia is based on the sound principles of the EU public procurement policies; it incorporates several transparency safeguards and competition instruments. However, the laws are not entirely comprehensive and several key elements of public procurement are individually regulated by the internal procurement policies of contracting entities. The regulatory framework could benefit from introducing higher accountability standards for contracting entities and contemporary eProcurement standards for communication and submissions should be further promoted.

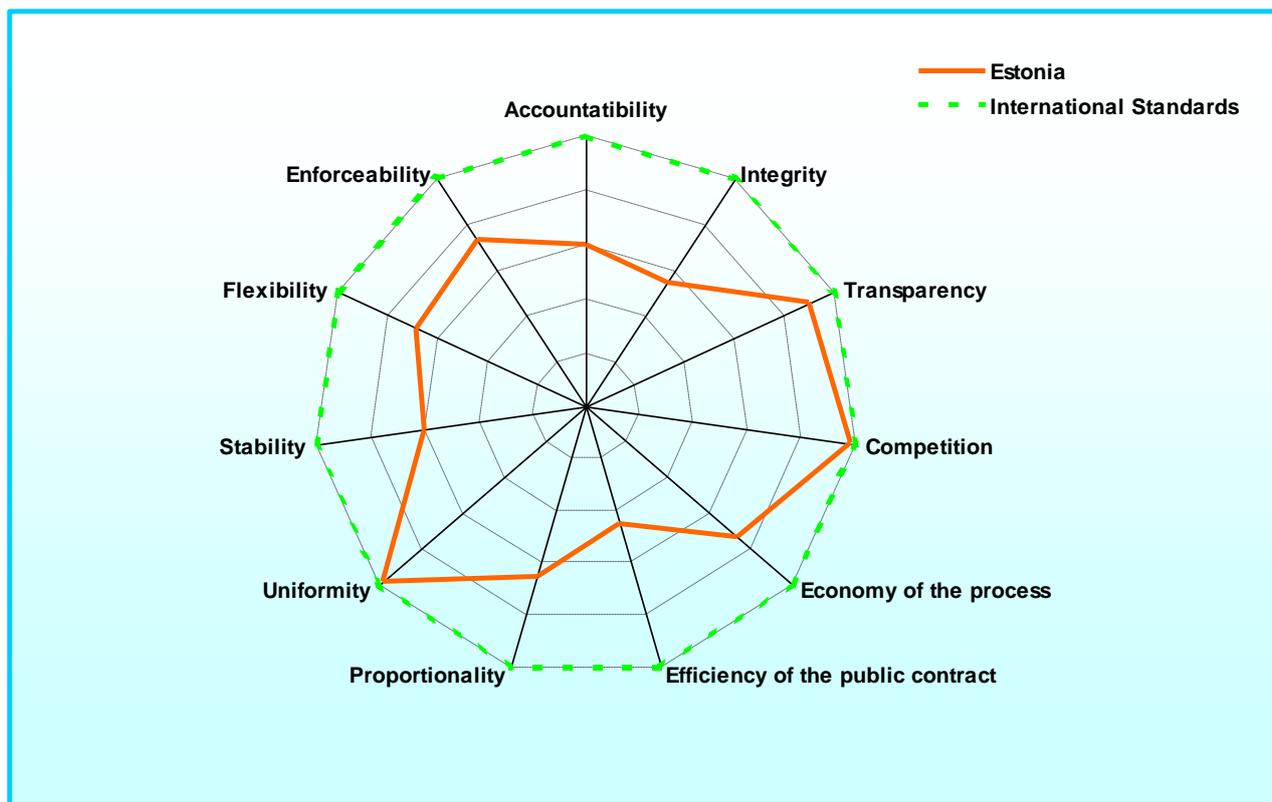
Chart 10 - Quality of Public Procurement legal framework in Estonia as compared to other EBRD countries of operation



Source: EBRD Public Procurement Assessment 2010

Note: The score represents the level of compliance of the country's legal framework with international standards such as the revised UNCITRAL Model Law on Public Procurements. Estonia is highlighted in comparison with other countries.

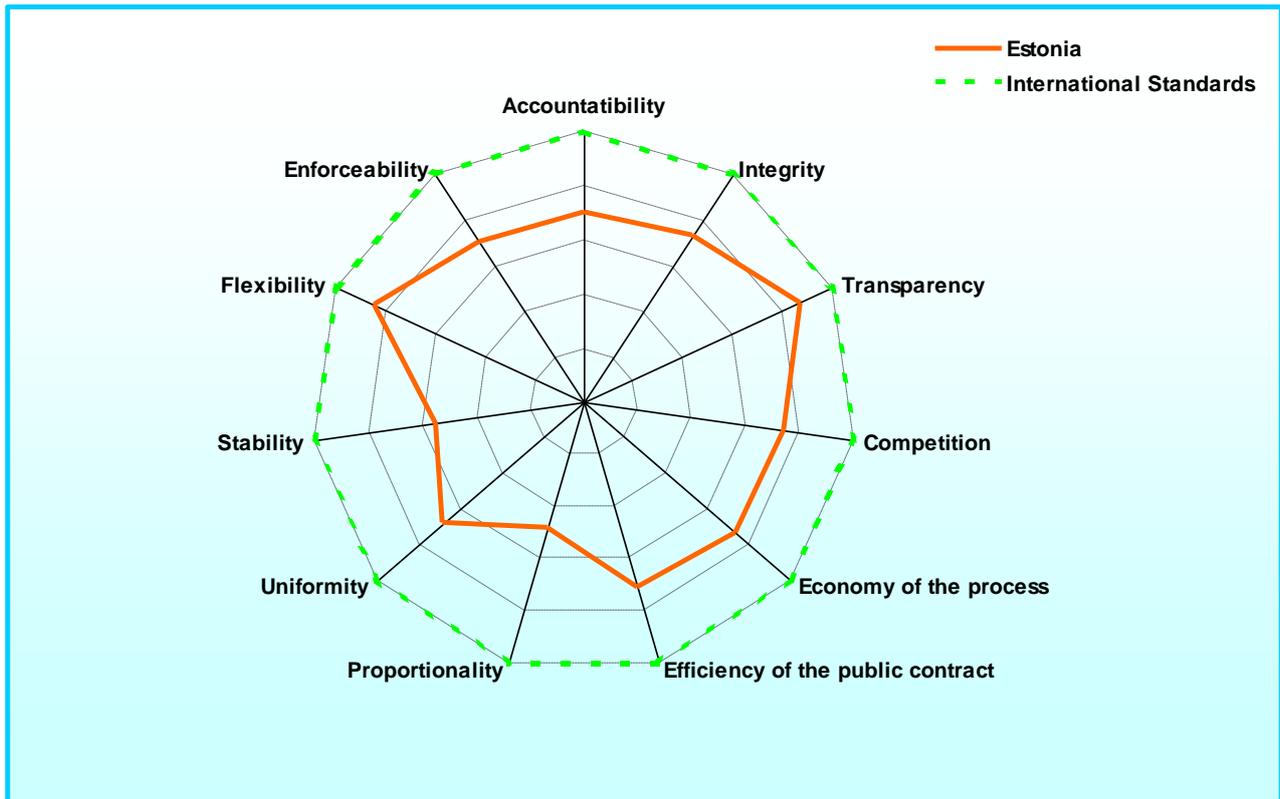
Chart 11 - Quality of Public Procurement legislation – Estonia (2010)



Source: EBRD Public Procurement Assessment 2010

Note: The extremity of each axis represents an ideal score in line with international standards such as the revised UNCITRAL Model Law on Public Procurement. The fuller the ‘web’, the more closely the public procurement laws of the country approximate these standards.

Chart 12 - Estonia - Quality of local procurement practice (2010)



Source: EBRD Public Procurement Assessment 2010

Note: The extremity of each axis represents an ideal score in line with international standards such as the revised UNCITRAL Model Law on Public Procurement. The fuller the 'web', the more closely the public procurement practices of the country approximate these standards.

3.6 Secured transactions

Secured transactions in Estonia are governed by the Law on Property and the Law on Commercial Pledge. These laws create a reasonably straightforward system of taking security on immovable property (mortgage) however the process of taking security over movable assets (pledge) remains rather complicated and in some aspects obsolete.

Mortgages are created by the registration of a notarised mortgage agreement or a notarised declaration of the owner's will to create a mortgage in the Land Register. A mortgage can secure any type of debt (present, conditional or future) up to the registered amount. The necessity to register the maximum amount of the secured debt is a slight downside of the system as it puts the creditor in a *pari passu* position with other unsecured creditors with potential surplus amounts of (un)secured debt. The Land Register is held by local courts under supervision of the Ministry of Justice. Mortgage rights enjoy priority upon registration. The database is centralised and fully electronic, and on-line searches of the Land Register can be made against the number or address of a property. However, the register is still not comprehensive as the land ownership reform has not been completed yet (which leaves buildings constructed on yet unregistered land outside of the system of taking mortgages).

Taking security over movable property and rights is rather complicated as different rules apply depending on the type of property or the parties involved. In order to create a pledge right according to the Law on Property, a transfer of possession of the collateralised asset is required.

Such a system does not satisfy the needs of modern commerce and restricts the use of movable property as a security. The Law on property also provides for taking security over rights (claims, accounts receivables, rights over real property, etc.). This security is also not registered and can be compared to conditional assignment as the sub-debtor of the claim has to be notified of the existence of the pledge and the creditor can enforce the pledge by receiving direct payment from the sub-debtor. According to the Law on Property, a non-possessory pledge can only be established and registered on movable assets whose title is already registered in a specific registry (*i.e.*, vehicles, aircraft, boats, intellectual property rights, etc.).

On the other hand, the Law on Commercial Pledge allows commercial enterprises to establish non-possessory “commercial pledges”, which encumber the whole of an enterprise. Such pledge has to be registered in the commercial pledge register. The non-possessory feature of the pledge allows a debtor to continue to use and dispose of the assets in the ordinary course of business. However, the system is fairly strict in that it does not allow the parties to define the collateral as they wish (*e.g.*, it cannot be established on specific assets) and can be used only by enterprises which are registered in the commercial register.

The concept of commercial pledge could be revisited and liberalised, especially if the main stakeholders express an economic need to do so.

3.7 *Securities markets*

The basic legal act regulating capital markets activities in Estonia is the Securities Market Act of 17 October 2001 (as amended). It established the regulatory framework for the operation of the Estonian securities market governing, *inter alia*, the provision of investment services, regulated markets and stock exchanges, initial public offering of securities, settlement of transaction with securities and other relevant matters. Other relevant legislation consists of: the Investment Fund Act of 2004 stipulating requirements regarding collective investment schemes; the Financial Supervisory Authority Act of 2002, consolidated text of 2011, providing legal basis for Financial Supervisory Authority (FSA) activities; the Money Laundering and Terrorism Financing Prevention Act (passed on 19 December 2007, entered into force in July 2011) establishing measures preventing money laundering and terrorism financing; Credit Institutions Act of -9 February 1999 (as amended), regulates activities of banks and other financial institutions. Furthermore, following Estonia’s accession to the euro zone the Act on the Adoption of the Euro was passed on 22 April 2010. The majority of the aforementioned legal acts implement relevant EU directives.

The securities market regulator is the FSA, which is competent for supervision of securities market operation, investment firms, credit institutions, collective investment schemes activities, insurance and pension funds. The FSA has the authority to issue advisory guidelines to securities markets legislation in order to provide guidance to subjects of financial supervision. The Tallinn Stock Exchange is the only regulated securities market in Estonia. It is part of the NASDAQ OMX Group.

All Estonian public limited company securities are registered in the Estonian Central Security Depository. Transactions with securities can be made using over-the-counter systems or regulated market. The regulated market operates in the context of a cross-Baltic stock exchange maintained by the NASDAQ OMX Group that coordinates the trading process and imposes regulations. Investors can enjoy simplified access and minimised investment barriers when operating on the Estonian market.

In the EBRD Securities Markets Sector Assessment 2007, the securities markets legislation in Estonia scored very well and was reported to be in high compliance with international best practice (see Chart 13). However, some implementation problems were reported, related to financial instruments regulation, money laundering, clearing and settlement (see Chart 14).

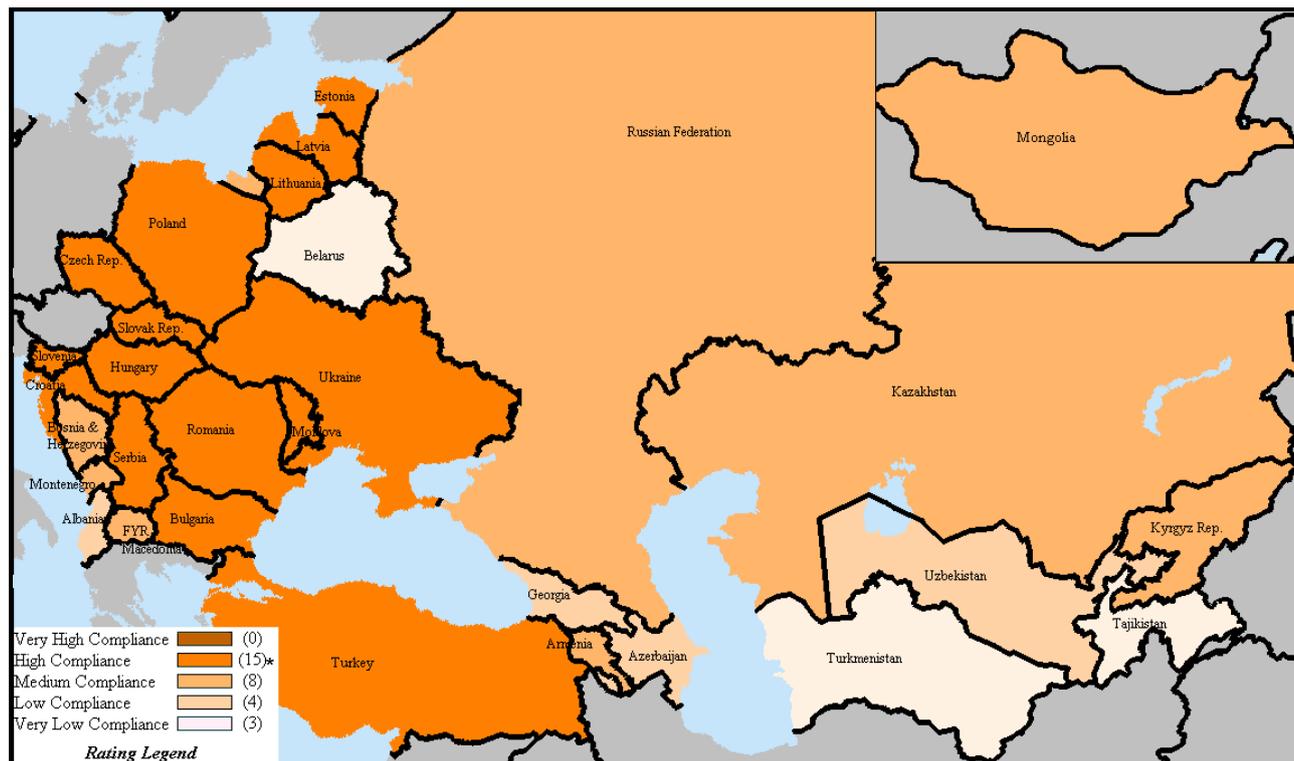
Despite recent developments related to Estonia's implementation of EU legislation, the Estonian capital market remains rather small and illiquid. The legal framework, however, is not an impediment to the market development since it implements various EU legislation, such as the Market in Financial Instruments Directive. There is, however, a weakness that should be addressed, i.e. the lack of a legal framework providing for close-out netting (*i.e.*, set-off in insolvency) and its enforceability (see Chart 14). Close-out netting is a standard in most developed jurisdictions (around 40 provide for it). Investors in derivatives or corporates hedging their exposure while entering into derivative transactions expect close-out netting to be enforceable.

Currently, the government is undertaking a four-year programme aimed at further boosting the country's competitiveness. This is to be achieved through lowering the tax burden and spurring job creation while preserving the current conservative fiscal approach. No reforms related to development of capital markets and relevant legal framework are included in the reform plan.

Two capital markets reforms related to the money market could be introduced. More specifically, close-out netting could be introduced in the Estonian legal framework and, moreover, a legal framework for classic repurchase agreements, in order to shift from current sell/buy back (reverse repos) transactions, could be clarified. Although there is a legal opinion addressing the enforceability of Global Master Repurchase Agreement, such agreements do not seem to be widely used.

Estonia was severely impacted by the financial crisis but the economy has been on a solid recovery path. As of 1 January 2011, Estonia is a member of the euro zone and it has implemented all EU legislation applicable to capital markets. Finally, a classic repo market could be further developed.

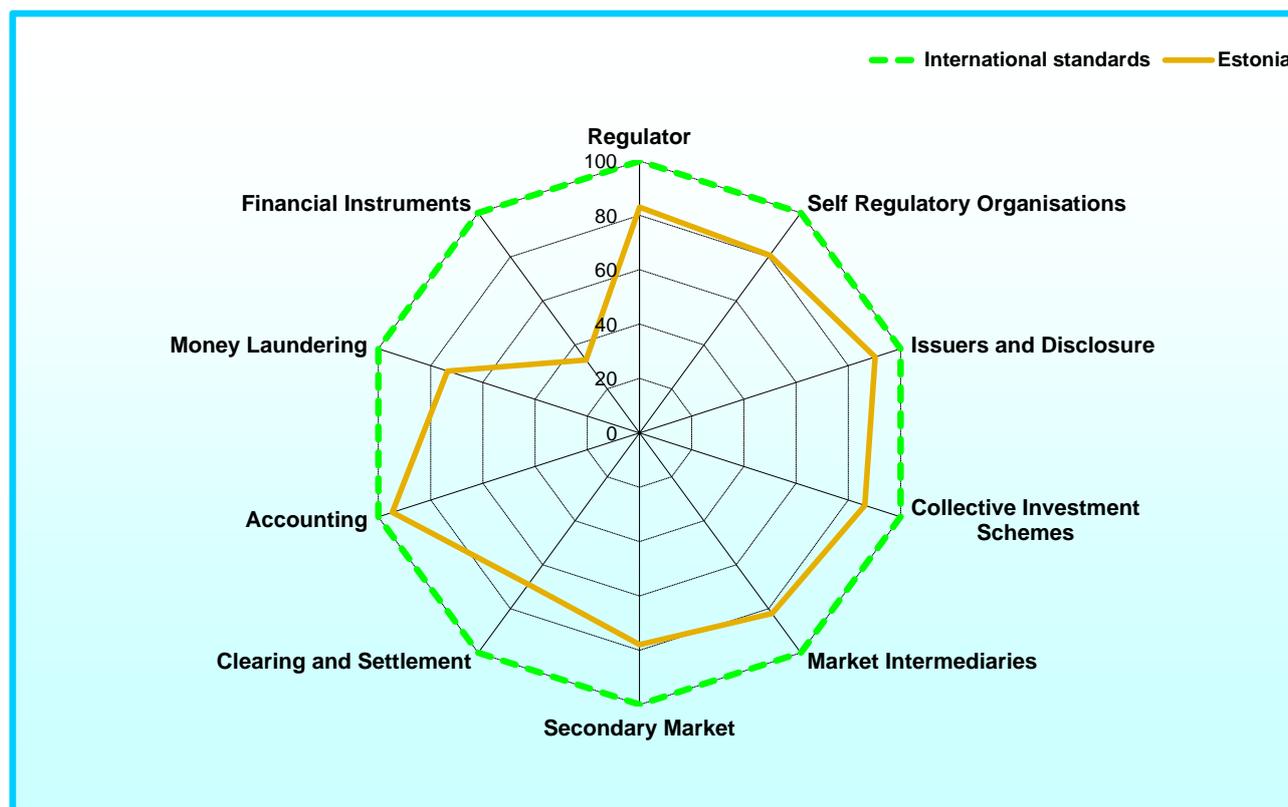
Chart 13 – Quality of securities markets legislation in the EBRD countries of operations



Source: EBRD Securities Markets Sector Assessment 2007

Note: The various categories represent the level of compliance of a given country’s legislation (the “laws on the books”) with international standards such as the IOSCO Principles. *The asterisk indicates in which category Estonia ranks.

Chart 14 – Quality of securities markets legislation in Estonia (2007)



Source: EBRD Securities Markets Sector Assessment 2007

Note: The extremity of each axis represents an ideal score in line with international standards such as the IOSCO Principles. The fuller the ‘web,’ the more closely the country’s securities markets laws approximate these standards.

3.8 Telecommunications / Electronic Communications

The electronic communications sector in Estonia is governed by the Law on Electronic Communications of 2005 (as amended) and supplemented by implementing regulations.

The Estonian market has been fully liberalised since January 2001 when the local, domestic, and international long-distance telephone markets were opened up to competition. Liberalisation of the market began soon after the country became independent and it remains one of the more advanced markets in Eastern Europe. As a member of the European Union (EU), Estonia is required to harmonise its sector legislation with the 2002 regulatory framework, as amended by the 2009 directives. Estonia notified its compliance with this requirement in time with the May 2011 deadline set by the European Commission. In the EBRD Telecommunications Regulatory Assessment 2008, the telecommunications regulatory framework of Estonia scored very well, in particular, in areas of wired and radio market access, SMP and safeguards, interconnection and special access as well as dispute resolution and appeal, each of which scored fully compliant with international best standards; regulatory independence, however, posed some concerns (see Chart 15). Since 2008 responsibility for regulation of the sector has been vested in two authorities, namely the Estonian Competition Authority (ECA) responsible for, among other topics, sector specific regulation, and the Estonian Technical Surveillance Authority responsible for spectrum, numbering and terminal issues.

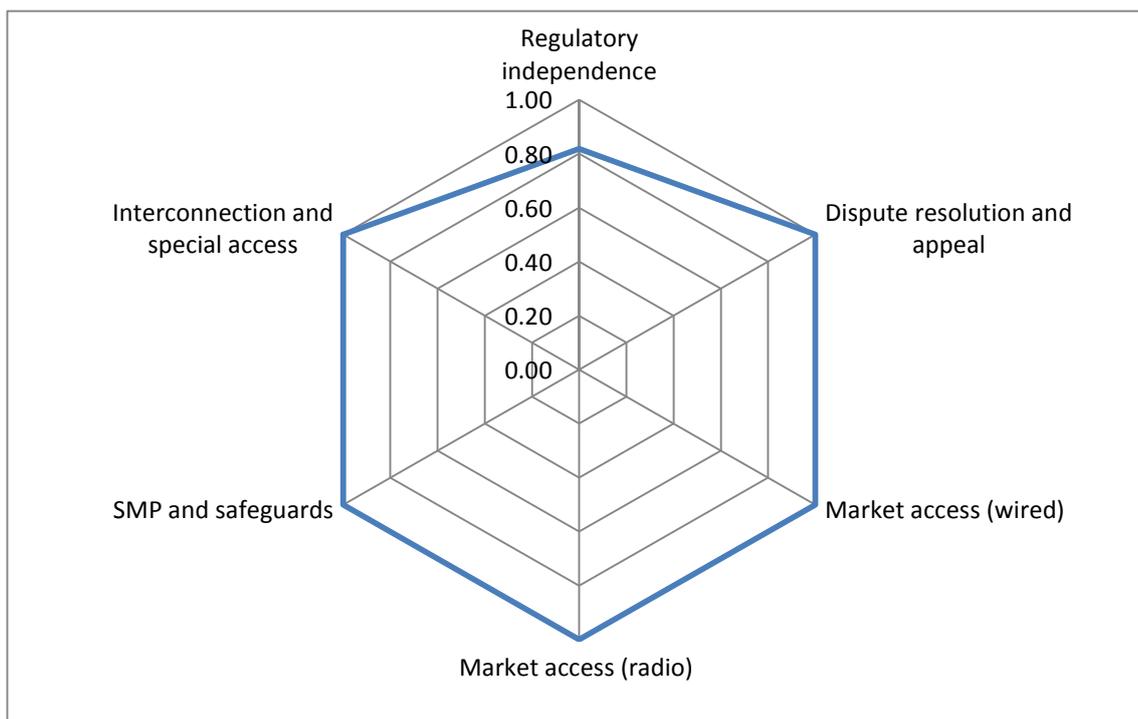
The progressive privatisation of incumbent operator, Elion was completed in January 2010, to TeliaSonera. Elion's share of the fixed market has been falling steadily in recent years and currently accounts for c. 60% of the market (see Chart 16(a)). Competition in the mobile market is intense, with penetration hovering around 120% (see Chart 16(b)). The largest operator (a subsidiary of incumbent Elion) continues to dominate the market with around 45% of the market, with its two competitors holding close to 25% each. The rest of the market is accounted for by MVNO. All three network operators have been granted 4G licences and are at varying stages of trial or commercial introduction of service.

While electronic communications is an important contributor to the Estonian economy in itself, it is the sector's role as an engine of growth and development across all sectors of the economy, together with its impact on societal issues that makes continued implementation of the ever evolving EU framework critical as a means of attracting the investment necessary to install next generation technologies that the development of the sector so much depend upon.

In common with other EU countries, Estonia has a national broadband plan, the 'EstWin' programme, which aims to eliminate the digital divide between the urban and rural areas, to increase social cohesion, and to contribute to economic growth. Approximately 22% of Estonian population has access to broadband (see Chart 16(c)). The government and private sector reportedly plan to invest about €300 million to build a country-wide broadband network capable of delivering 100 Mbps connections to the majority of Estonian households and businesses by the end of 2015, in accordance with EU aspirations in this respect.

As with all modern economies, Estonia's key sector challenge is the roll-out of next generation broadband networks with sufficient capacity to underpin the government's (and the EU's) information society and knowledge economy objectives. In doing so, the government must be careful to sufficiently balance the interests of the consumer through maximising the shorter term benefits of price, choice and quality that full competition can bring with the interests of private investors with sufficient incentives to invest in costly new generation infrastructure. While Estonia's small size, advanced market and the firm basis that the EU framework provides will greatly aid the government in their approach, they should nonetheless tread carefully in this respect.

Chart 15 – Quality of telecommunications regulatory framework in Estonia (2008)

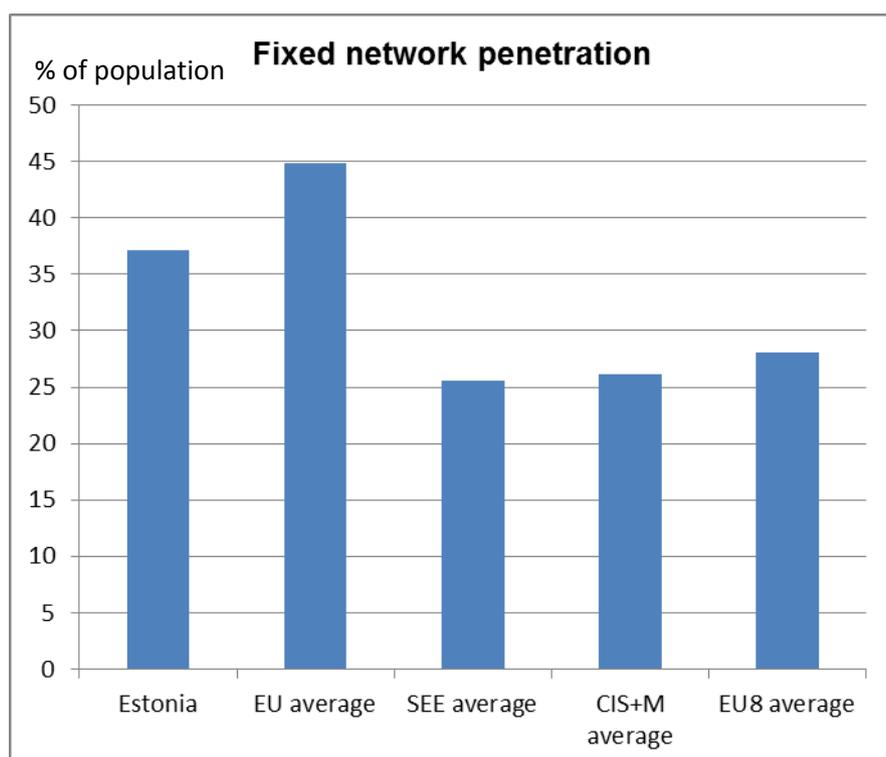


Source: EBRD Telecommunications Regulatory Assessment 2008

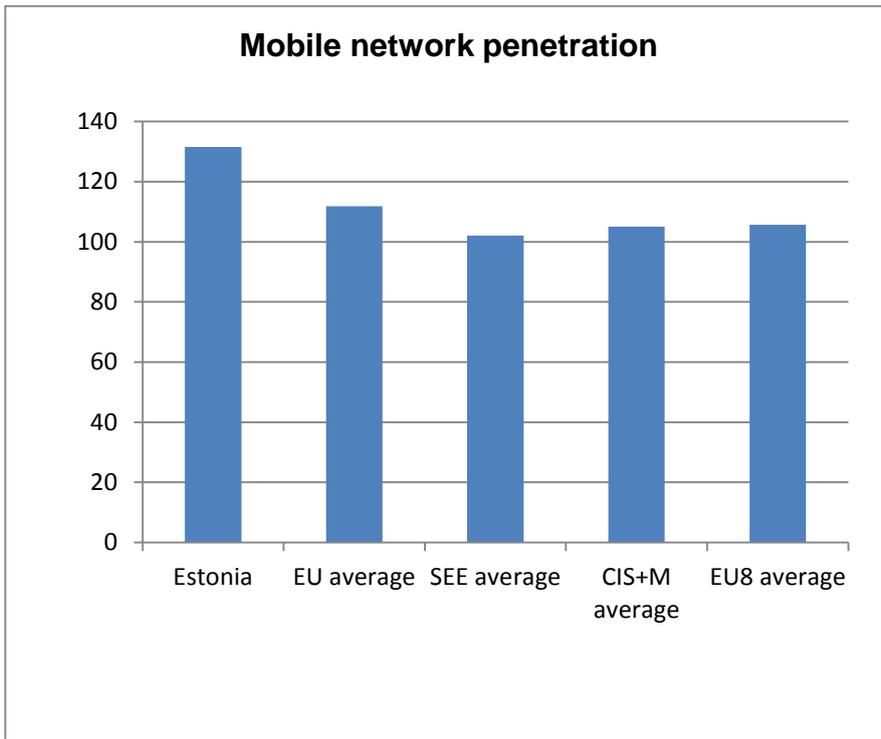
Note: The diagram shows the combined quality of institutional framework, market access and operational environment when benchmarked against international standards issued by the WTO and the European Union. The extremity of each axis represents an ideal score of 100 per cent, that is, full compliance with international standards. The fuller the “web”, the closer the overall telecommunications regulatory framework of the country approximates these standards.

Chart 16 – Key indicators for Estonia (2008)

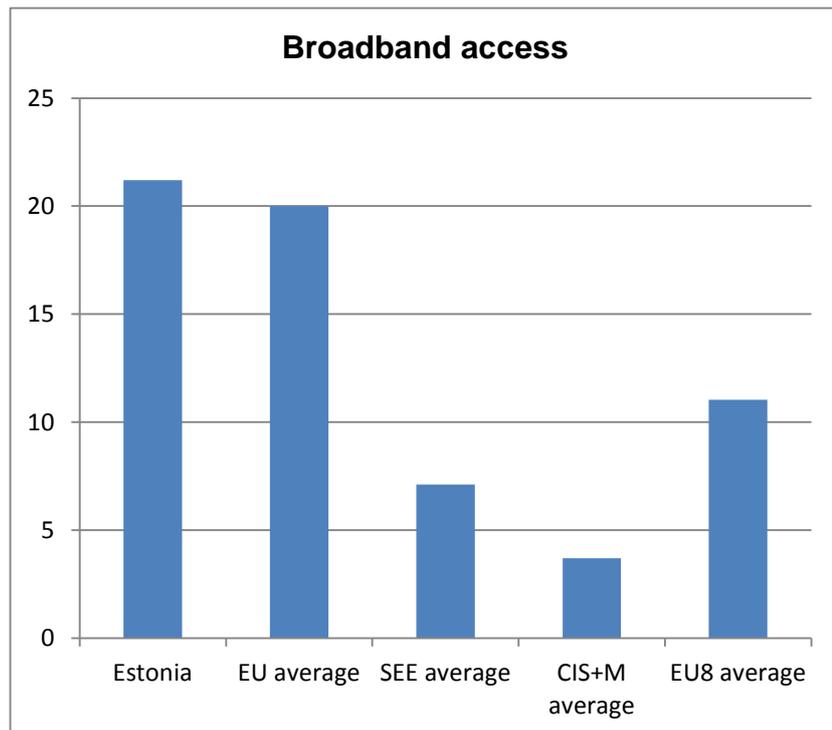
16(a) Fixed Network Penetration



16(b) Mobile Network Penetration



16(c) Broadband Network Penetration



Source: EBRD Telecommunications Regulatory Assessment 2008

Note: Key indicators for Estonia provide the fixed network penetration defined as active subscriber lines as a percentage of population, mobile network penetration defined as active pre- and post-paid subscribers as a percentage of population and the broadband network penetration defined as the number of access subscribers with speeds of 144k/bits or more as a percentage of population (broadband Network Penetration less than 1% is not shown on this chart).