



Dear reader,

The fact that you are holding in your hands the 15th edition of *Juridica International* demonstrates the viability of the law journal of the University of Tartu and the success of the endeavour that started in 1996. The fastidious prior review of contributions has justified itself; over the years, our publication has become a highly valued channel for Estonian jurists for taking their research to the international arena. To our delight, foreign colleagues are publishing their articles in the journal with increasing frequency.

The general subject of this edition is “Estonia in the European Union: Creation and Implementation of New Laws”. The Republic of Estonia, which is celebrating its 90th anniversary, has had to repeatedly prove itself when restoring independence and building up statehood. Membership in the European Union since 2004 finalised Estonia’s formal return to where it really belongs — the family of Western democracies. Effective affiliation with the European cultural and legal area and the Europeanization of various areas of life is an ongoing process. The development of Estonian law to meet European standards requires continued efforts from our jurists and lawyers. This is a great and common task composed of the contributions of many persons in their respective specific fields, which eventually takes forward not only Estonian, but also European Union law.

The articles in this edition cover a wide range of topics, all of which are integrally related to the newest developments in the Estonian legal sphere. The first group of articles (by Hannes Veinla, Lasse Lehis, Inga Klauson, Helen Pahapill, Erki Uusitalu, Merle Muda) are dedicated to the introduction of the principles of European Union directives into Estonian environmental law, tax law and labour law. The next group of articles relate to the harmonisation of private law in the European Union Member States and Estonian company law (authors Karin Sein, Mari Ann Simovart, Kalev Saare, Kadri Siibak, Age Värvi, Luboš Tichý, Margit Vutt, Andres Vutt). The group of articles focusing on specific branches of law deal with Estonian economic law, copyright law, procedural law, criminal law, and legal sociology (authors Katri Paas, Aleksei Kelli, Anneli Alekand, Paavo Randma, Silvia Kaugia). The edition closes with articles about the contacts between Estonian and international law in the context of the events of April 2007, as well as about the history of Baltic law and about Estonian legal terminology (authors René Värk, Arnold Sinisalu, Hesi Siimets-Gross, Merike Ristikivi). The pervading idea of all the articles is to identify how the various areas of law continue to transfer from totalitarian to democratic and in which direction international law is developing. Most of the articles reflect how the specific Estonian conditions have been taken into account in the general European Union framework of implementation of legislation and law.

The relationship between law and real life is like walking on two feet, because one can steadily move in a certain direction only when both feet work in synchrony. It is not always important whether the law or reality takes the first step; it is important to have a steady orientation. And, of course, one foot should not push too far ahead when the other is faltering, as that would mean moving in a circle. This gives the impression of speed without any actual progress. Hopefully the articles in this edition of *Juridica International* demonstrate convincingly that Estonian law and real life are developing in good harmony and following the same direction, and that nobody has to worry about the clarity of the goals.

Finally, we would like to thank the Ministry of Justice whose financial support greatly conduced to the publication of this edition.

Jüri Saar

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Scope and Substance of the Integration Principle in EC Law and Its Application in Estonia

1. Introduction

The integration principle has been recognised as one of the cornerstones of modern environmental policy and law.

Principle 4 of the Rio Declaration on Environment and Development^{*2} as adopted by the United Nations Conference on Environment and Development in Rio de Janeiro in 1992 proclaims the following:

In order to achieve sustainable development, environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it.

According to the Amsterdam Treaty, the integration principle is now stipulated in Article 6 of the EC Treaty, which goes further than the Rio Declaration and prescribes that:

Environmental protection requirements must be integrated into the definition and implementation of the Community policies and activities referred to in Article 3, in particular with a view to promoting sustainable development.

The integration of environmental concerns into other areas of policy has achieved the status of one of the basic principles of EU environmental policy and law. As stated above, the principle is reflected in Article 6 of the EC Treaty, the very frontispiece of the treaty. This indicates that the principle has a general character and affects all policy areas. The European Court of Justice has ruled, in the case *Greece v. Council*^{*3}, that it is a binding obligation and that environment-related requirements must be integrated into the other policies, but it is still far from clear what constitutes the exact substance of this principle.^{*4}

¹ This article was published with support from ESF Grant No. 6673.

² Available at <http://www.unep.org/Documents.Multilingual/Default.Print.asp?DocumentID=78&ArticleID=1163> (12.05.2008).

³ Case 62/88, paragraph 20. Available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:61988J0062:EN:HTML> (11.05.2008).

⁴ See also R. Wurzel. The EU Presidency and the Integration Principle: An Anglo German Comparison. – European Environmental Law Review, January 2001, pp. 13–14.

There are numerous uncertainties as to how to understand the integration principle. What is its object (as reflected in the language “policies and activities” and “definition and implementation”), who are the addressees (the Community or also Member States insofar as implementation of EU policies is concerned), and what are the criteria (“environmental protection requirements”, “with a view to promoting sustainable development”)? There are also doubts as far as character of guidance (“must be integrated”) is concerned — is it enabling authorities to restrict economic activities, or is it directing authorities to introduce such restrictions? Does the integration principle constitute a procedural or substantive prescription?

The present article seeks answers to some of these questions and explores how the integration principle is transposed into Estonian legislation and legal practice.

2. The integration principle in EU law

2.1. The object and addressees of the integration principle

On the EU level, the integration principle plays a role in policy-making and adoption of legislation in all policy areas indeed. Before the Amsterdam Treaty, the integration principle was stipulated in Article 174 of the environmental chapter of the EC Treaty. The principle was formulated similarly to one used now in Article 6.⁵ L. Krämer notes that, before the Amsterdam language was formulated, there was active debate about the method for reflection of the integration principle in the EC Treaty. There were two basic concepts. The first was to incorporate a reference to environmental considerations into other chapters of the EC Treaty, such as chapters on agricultural, transport, competition, and other policies. The second was to reflect the principle in the general part of the treaty. In Amsterdam, the second option prevailed.⁶ The interpretation of the integration principle makes it quite clear that this principle covers both policies and activities as well, and also the definition and implementation of any policies that are within EC competence.

The principle should be interpreted in such a way that environmental policy cannot be viewed in isolation as a specific policy sector alone. Environmental policy should be horizontal and cover all areas with environmental impact.

Furthermore, the integration principle covers not only definition and implementation of all policies having even remote impact on the environment but also individual activities. The integration principle has achieved the status of a general principle of Community law.

The requirement for integration is not met with the same strength in any of the other areas of policy in the European Union. Also, in Article 37⁷ of the Charter of Fundamental Rights of the European Union it is prescribed that:

A high level of environmental protection and the improvement of the quality of the environment must be integrated into the policies of the Union and ensured in accordance with the principle of sustainable development.

J. Jans, one of the most distinguished scholars of EU environmental law, believes the requirement for the integration of environmental considerations to be the most important provision concerning the environment in the EC Treaty.⁸ Indeed, Article 6 of the EC Treaty, along with Article 37 of the Charter of Fundamental Rights of the European Union, gives environmental protection a whole new meaning in the EU context. Now there is no longer any area of policy (including law) influencing the state of the environment where environmental concerns do not have to be taken into consideration. With the aid of the integration principle, entry of environmental considerations into nearly all fields of human activity is occurring. This tendency, sometimes called ecological modernisation, follows the idea that economic and social development are not allowed to be, and should not be, a cause of environmental damage. In certain cases, economic and social development may bring with them even an improvement in the quality of the environment.

As an example of integration, fisheries policy can be highlighted. A fishery falls within the exclusive competence of the EC. The basic legal source regulating fisheries policy is Regulation 2371/2002.⁹ The regulation defines sustainable use of fish resources in Article 3 (e):

⁵ “Environmental protection requirements must be integrated into the definition and implementation of other Community policies.”

⁶ See L. Krämer. *EC Environmental Law*. 6th edition. London: Sweet and Maxwell 2007, p. 21.

⁷ For more information about this article, see F. Ermacora. *The Right to a Clean Environment in the Constitution of the European Union. – The European Convention and the Future of European Environmental Law*. J. Jans (ed.). Groningen: Europa Law Publishing 2003, pp. 29–42.

⁸ See J. Jans. *European Environmental Law*. Kluwer Law International 1999, p. 25.

⁹ Available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2002:358:0059:0080:EN:PDF> (12.06.2008).

‘Sustainable exploitation’ means the exploitation of a stock in such a way that the future exploitation of the stock will not be prejudiced and that it does not have a negative impact on the marine ecosystems.

At least in theory, this is a rather strong version of integration, because strict substantive criteria are used; implementation of fisheries policy must not have a negative impact on marine ecosystems as a whole.

Where the addressees of the principle are concerned, the academic debate is focused on the question of whether the principle is binding only on the Community level and for Community institutions. Alternatively, is it binding also for Member States? For example, L. Krämer insists that Article 6 is addressed merely to Community institutions.^{*10} The author of the present article cannot fully agree with this statement. The principle seems to be addressed not only to the EC; it appears to bind also, at least indirectly, Member States. The implementation of EC environmental policy is a responsibility of Member States; consequently, Member States should take care of integrating environmental concerns into policies and activities in order to achieve a high level of protection, taking into account the principle set forth in Article 10 of the EC Treaty. This article prescribes that:

Member States shall take all appropriate measures, whether general or particular, to ensure fulfilment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community. They shall facilitate the achievement of the Community’s tasks.

Article 2 of the EC Treaty reflects the main tasks of the Community:

The Community shall have as its task, by establishing a common market and an economic and monetary union and by implementing common policies or activities referred to in Articles 3 and 4, to promote throughout the Community a harmonious, balanced and sustainable development [...] a high level of protection and improvement of the quality of the environment [...].

Consequently, Article 10 in conjunction with Article 2 of the EC Treaty commands Member States to achieve a high level of environmental protection. This cannot be obviously achieved without integrating environmental concerns into policies and activities potentially affecting the environment.

2.2. What should be integrated?

Article 6 of the EC Treaty prescribes that environmental protection requirements must be integrated into the definition and implementation of the Community policies and activities. “Environmental protection requirements” means measures needed to ensure a high level of environmental protection. Furthermore, the environmental protection requirements referred to in Article 6 may be considered to encompass the objectives, principles, and conditions for action mentioned in Article 174 of the EC Treaty, as well as all other environmental protection principles, guidelines, and criteria that may be derived from the EC secondary environmental legislation and the relevant EC case law as well. One of the prescriptions that should enter into policies in other fields should be the precautionary principle in the event of scientific uncertainty. The precautionary principle is among the primary legal means by which environmental protection and sustainable development are achieved at an advanced level. Putting precaution into practice is an administrative task allowing for setting of ambitious environmental goals in such a manner that substantiating their legitimacy does not require final proof of potential environmental damage.^{*11}

The integration principle is ultimately related to the principle of sustainable development. There are different opinions as to what the legal content of sustainable development is. According to my understanding, instruction to integrate environmental consideration into other fields is one of the legal aspects of the principle of sustainable development. One of the most widely recognised German scholars of the precautionary principle, S. Boehmer-Christiansen has treated the precautionary principle as one of the most important methods used in achieving sustainable development, which places the responsibility for the protection of the natural foundation of life for current and future generations with the government and gives government the right to intervene in the structure of the liberal consumption society with its short-term perspective.^{*12}

¹⁰ L. Krämer. *EC Environmental Law*. London: Sweet and Maxwell 2003, p. 11.

¹¹ See E. Fisher. *The Precautionary Principle As a Legal Standard for Public Decision-making: The Role of Judicial and Merits Review in Ensuring Reasoned Deliberation*. – Perspectives on the Precautionary Principle. R. Harding, E. Fisher (eds.). Federation Press 1999, p. 90.

¹² See S. Boehmer-Christiansen. *The Precautionary Principle in Germany: Enabling Government*. — Interpreting the Precautionary Principle. T. O’Riordan, J. Cameron (eds.). London: Earthscan 1994, p. 55.

2.3. Character of guidance — “must be integrated”

Article 6 is not the only integration clause in the EC Treaty. But there is still a clear difference. The phrase “must be integrated” appears in Article 6 as a stronger expression than those used, for example, in Articles 127 and 153 of the EC Treaty. These articles concern employment and consumer protection policies, respectively, and state that the objective of a high level of employment “shall be taken into consideration” and consumer protection “shall be taken into account”. Article 6 is obviously more demanding.

The integration principle does not merely enable^{*13} relevant authorities to restrict economic activities if this is necessary for achieving a high level of protection. It also commands them to do so if it is necessary. At the same time, the integration principle leaves to the institution very broad room for discretion concerning what kind of environmental requirements are involved and to what extent to perform integration. Similarly to the achievement of a high level of environmental protection, integration does not necessarily mean precedence over other policies.^{*14}

Because of the considerable room for discretion, court control is obviously limited. A court can probably intervene and correct only in cases in which there is a clear and manifest disregard for environmental concerns. In implementation of the integration principle, other general principles of law should be taken into account as well — first of all, the principle of proportionality. This means that environmental concern shall not have *prima facie* supremacy over other considerations. The integration principle commands that environmental concerns be taken into account and carefully and prudently considered.

2.4. Procedural or substantive character of the integration principle

The integration principle set forth in Article 6 of the EC Treaty clearly has not only procedural but also substantive content. It is not merely the requirement to take environmental considerations into account; it instructs to achieve a certain environment-related result — a high level of protection: a measure may not cause environmental damage that cannot be outweighed by other, prevailing reasons.

It is not easy to answer the question of what constitutes a high level of environmental protection. In the literature, it has been stated that this probably means the level achieved by ‘environment-friendly’ Member States such as Sweden, Denmark, Finland, Austria, and Germany.^{*15} In general, the author agrees with that position and considers it necessary to add that, under Article 95 (7) of the EC Treaty, such Member States can also contribute to improving the ‘level’ of harmonisation measures. Namely, Article 95 of the EC Treaty provides for those derogations when a Member State may introduce and apply environmental requirements that are more stringent than the harmonisation measures. The above-mentioned Article 95 (7) provides that when “pursuant to paragraph 6, a member state is authorised to maintain or introduce national provisions derogating from a harmonisation measure, the Commission shall immediately examine whether to propose an adaptation to that measure”. In explanation, the European Commission must consider whether to raise the level of harmonisation measures and establish environment-related requirements that are stricter than the existing ones.

The author is of the opinion that there are still even more indicators of a high level of environmental protection. I consider these to be primarily the application of the precautionary principle and the principle of integration.

That a high level of protection requires the application of the precautionary principle has also been found by the court of first instance in *Artegodan v. Commission*.^{*16} The company Artegodan had a licence to manufacture medicinal products containing amfepramone. On 9 March 2000, the European Commission adopted three decisions to prohibit that substance on the basis of the opinion of a number of scientists and doctors that, under certain circumstances, medicinal products containing that substance could pose a potential risk to health. The company contested those decisions, relying on the principle of proportionality. At this point, I would like to highlight the following section of the court’s judgment. The court pointed out that the precautionary principle should be applied not only to achieve a high level of environmental protection but also to ensure a high level of health and consumer safety. Thus, the court pointed out that, in order to achieve a high level of protection, the precautionary principle must be applied and, also, uncertain risks must be prevented.^{*17}

¹³ G. Winter distinguishes enabling and directing function of the principles. See G. Winter. *Environmental Principles in Community Law. – The European Convention and the Future of European Environmental Law*. J. Jans (ed.). Groningen: European Law Publishing 2003, pp. 4–7.

¹⁴ See *Germany v. Parliament and Council*, Case C-233/94.

¹⁵ L. Krämer (Note 10), p. 11.

¹⁶ *Artegodan GmbH v. Commission*, Case T-74/00, paragraph 183. Available at <http://curia.eu.int/jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&nomusuel=Artegodan&resmax=100> (11.05.2008).

¹⁷ *Ibid.*

3. The integration principle in Estonian law and practice

3.1. The integration principle in the Constitution and framework environmental legislation

3.1.1. The Constitution

There are two provisions in the Estonian Constitution that could be, at least indirectly, related to the principle of integration. Section 5 of the Constitution stipulates that:

The natural wealth and resources of Estonia are national riches which shall be used sustainably.

In the case *Koidu Park*, the Tallinn district court^{*18} directly referred to § 5 in the context of the integration principle. The case will be dealt with in more detail below.

Furthermore, § 5 of the Constitution can also be interpreted in such a way that integration of environmental protection requirements constitutes valid legal grounds to justify encroachment on basic entrepreneurial and property rights and freedoms and to limit the environmental impact of economic activities.

Section 53 of the Constitution stipulates that:

Everyone has a duty to preserve the human and natural environment and to compensate for damage caused to the environment by him or her.

Unfortunately, there is still no court practice addressing § 53, but, in my opinion, this provision can be interpreted in such a way that a certain environment-related ‘duty of care’ must be integrated into all activities affecting the environment.

3.1.2. Framework legislation

Three sources can be brought forward in this case — the Act on Sustainable Development^{*19}, the Planning Act^{*20}, and the Nature Protection Act.^{*21}

Subsection 3 (3) of the Sustainable Development Act stipulates the following:

Minimisation of environmental pollution and use of natural resources should be considered to be basic requirements of all economic activities.

This subsection is very broad and general, but nevertheless it could be interpreted in such a mood that environmental concerns must be integrated not only into legislation but also in economic practices. At the same time, this provision creates several questions — of exactly what should be integrated and to what extent. Unfortunately, there are no clear answers to such questions, neither in Estonian legislation nor in court or even administrative practice. Estonian law obviously leaves a very broad margin for discretion here.

Section 12 of the Sustainable Development Act prescribes:

Development of economic sectors and areas where environmental pollution or use of natural resources may have negative environmental impact should be governed by development plans. Such plans should be drawn up with respect to the sectors of energy, transport, agriculture, and forestry and to the chemical, building material, and food industries.

This is one of the few highly practical provisions of the otherwise very vague Sustainable Development Act. Just such development plans indeed have been drawn up. One of the primary functions of these plans is integration of consideration for the environment into other policies. The problem, however, is that these plans are only indirectly binding on the administration and in too many cases are not seriously considered and taken into account in the taking of individual decisions.

The purpose of the Planning Act is to “ensure conditions that take into account the needs and interests of the widest possible range of members of society for balanced and sustainable spatial development, spatial planning, land use, and building”. According to § 2 (2) of the act:

¹⁸ Tallinn District Court, 18.04.2008, 3-06-1136. Available at <http://www.kohus.ee/kohtulahendid/temp/3-06-1136.pdf> (12.06.2008) (in Estonian).

¹⁹ Säätstva arengu seadus. Adopted on 22.02.1995. – RT I 1995, 31, 384 (in Estonian).

²⁰ Planeerimiseseadus. Adopted on 13.11.2002. – RT I 2002, 99, 579 (in Estonian).

²¹ Looduskaitse seadus. Adopted on 21.04.2004. – RT I 2004, 38, 258 (in Estonian).

[...] spatial planning is democratic and functional long-term planning for spatial development that co-ordinates and integrates the development plans of various fields and, in a balanced manner, takes into account the long-term directions in and needs for the development of the economic, social, cultural, and natural environment.

As one can see, the main purpose of the land use planning procedure is to ensure sustainable development — balancing of economic, social, cultural, and environmental considerations (values). Unfortunately, this idea is a bit idealistic in Estonian conditions. Estonia is famous for its ultraliberal economic policy, and in reality in most cases where there is certain conflict between different interests — economic and environmental, for instance — the economic considerations prevail. This is a general problem of the legal culture. Most Estonian environment-related laws are very progressive, but at the stage of implementation the ‘power’ of environmental law weakens considerably.

In the Nature Protection Act, one can find a framework provision that could somehow be linked with the integration principle. Subsection 2 (2) of the act prescribes that:

Nature conservation shall be based on the principles of balanced and sustainable development and in each individual case, alternative solutions shall be considered which, from the position of nature conservation, are potentially more effective.

This provision indirectly refers to the integration principle and orders — when environment-related decisions are taken, that the alternative that is ‘best for the environment’ always be carefully considered. Unfortunately, there have been no court cases dealing with this matter in Estonia yet.

3.1.3. Draft legislation

The Coalition Agreement of the government (from May 2007) sets up a goal of codifying Estonian environmental law.^{*22} The first step in this obviously lengthy process will be elaboration of the ‘General Part Act’ for the Estonian Environmental Code. At the moment, Estonian environmental law lacks such a general framework act; Estonian environmental law is fragmented and organised by sectors. This deficit obviously weakens the impact of environmental regulation and negatively affects also integration of environmental requirements into other policies.

One of the chapters of the draft deals with planning of environmental protection — in particular, strategies and action programmes in the field of the environment. There will be envisaged three types of strategies — national long-term environmental strategy, strategies of different areas of environment protection (e.g., nature conservation strategy, forest policy, etc.), and so-called strategies of integration (energy, transport, tourism, etc.). All of these strategies deal in some way with integration tasks, but the last will be specially designed to promote integration of environmental concerns.

3.2. The integration principle in policy papers

The Estonian National Strategy on Sustainable Development called Sustainable Estonia 21 was approved by the Estonian Parliament in September 2005.^{*23} The strategy focuses on the concept of sustainability for the long-term development of the Estonian state and society until the year 2030. The general development principle for the country is “to integrate the requirement to be successful in global competition with a sustainable development model and preservation of the traditional values of Estonia”.

The strategy defines Estonian long-term development goals of taking into consideration interaction between environmental and development factors:

- Viability of the Estonian cultural space: According to the Constitution of the Republic of Estonia, the state of Estonia shall “ensure the preservation of Estonian nature and culture through the ages”.^{*24} The sustainability of the Estonian nation and culture constitutes the cornerstone for the sustainable development of Estonia.
- Enhancement of welfare: Welfare is defined as the satisfaction of the material, social, and cultural needs of individuals, accompanied by opportunities for individual self-actualisation and for realising one’s aspirations and goals.
- Coherent society: Achievement of the first two goals will be possible only if the benefits proceeding from their realisation can be enjoyed by the majority of the population and the price for achieving the goals is not destructive for the society as an integral organism. Realisation of the goals is possible

^{*22} Available at http://www.valitsus.ee/failid/2007_12_20_VV_tegevusprogramm_LOPLIK.pdf (12.06.2008) (in Estonian).

^{*23} Available at http://www.riigikantselei.ee/failid/Saastev_Eesti_21.pdf (12.06.2008) (in Estonian).

^{*24} Eesti Vabariigi Põhiseadus. Adopted on 28.06.1992. – RT 1992, 26, 349; RT I 2007, 33, 210 (in Estonian).

only in a situation where an absolute majority of the members of society believe in and contribute to their achievement — i.e., in a coherent and harmoniously functioning society.

- Ecological balance: Maintenance of ecological balance in the natural environment of Estonia is a central precondition for our sustainability. It is also a contribution to global development, following the principle that requires a balance both in cycles of materials and in flows of energy at all levels of the living environment.^{*25}

The strategy emphasises that the overall aim is to integrate considerations related to the regenerative capacity of nature into the use of nature. The main function of environmental protection is not to protect resources and the natural environment but to achieve their harmonious and balanced management in the interests of Estonian society and local communities. The aim is to reach a situation where humans regard the environment not as a pool of objects requiring protection but as an integral whole of which the human is one part. The aim is combined conception of nature as a value and as a central development resource of the society in the context of the overall development of Estonia.

In my opinion, the strategy clearly uses the language of ‘integration’, but from the other side it concentrates too much on economic and social issues, with environmental concerns still somehow subordinated to these. The other problem with regard to the strategy is another connected with Estonian legal culture. Such policy documents do not play a significant part ‘in real life’ and are very frequently disobeyed when legislative or executive decisions are taken.

3.3. Interpretation of the integration principle by the judiciary

There are two indeed significant cases of the Estonian courts that are related to the integration principle — the so-called *Jämejala Park* case^{*26} of the Estonian Supreme Court and, already mentioned, the *Koidu Park* case.

A historic and well-preserved park can be found in a small village — Jämejala — in central Estonia. In Soviet times, a hospital for mentally disabled people was erected in the park. In the late 1990s, the Ministry of Justice launched a project to construct on the basis of the existing building a new central hospital for prisons. The planned new facility would have needed more space, and, as a consequence, a significant part of the park would have had to be destroyed. Under Estonian planning law, all such projects should be based on a land use plan. The plan was initiated and subsequently adopted by the local government. Adoption of a land use plan is under Estonian law a discretionary decision that should entail weighing of different interests and values. The decision of the local government was based on two arguments. The first argument was brought out by the Ministry of Justice — building of a new facility in the park on the basis of existing buildings would have resulted in fewer costs. The local government emphasised the opportunity for new jobs for local people, who suffered from a high rate of unemployment. When deciding on the plan, the local government totally ignored the environmental value of the park, which was brought up in discussion by local people, who decided to protect the park. A group of local residents filed a complaint with the administrative court and contested the adoption of the planning, applying for annulment of the administrative act. The court of first instance and the district court dismissed the complaint, but the Supreme Court took a different position. The Supreme Court annulled the plan. The court’s reasoning here was based on the concept of discretion. Under Estonian administrative law, the right of discretion is an authorisation granted to an administrative authority by law to consider making a resolution or choose between different resolutions. The right of discretion shall be exercised in accordance with the limits of the authorisation, the purpose of discretion, and the general principles of justice, taking into account all relevant facts and considering all legitimate interests. The Supreme Court pointed out that the planning act adopted by the local government was not based on all relevant facts and consideration of all legitimate interests. In the Supreme Court’s estimation, the local government totally ‘forgot about’ environmental considerations and this should be considered a manifest error of discretion that should lead to a declaration of illegality of the planning decision.

As a conclusion, it could be said that in the latter case the Estonian Supreme Court used the integration principle in the context of the right of discretion of administrative bodies. The court emphasised that environmental consideration should always be taken into account in decisions on development plans or projects that can have a negative environmental impact. This decision seems to be a quite effective interpretation of the integration principle. The Estonian Supreme Court pointed out that environmental concerns should have significant legal weight and that they can and must successfully compete with economic and social concerns. Furthermore, the court added that weighty arguments are not only those concerning environment-related

²⁵ See Web site of Estonian Ministry of Justice at <http://www.envir.ee/58738> (11.05.2008).

²⁶ Estonian Supreme Court, 14.10.2003, 3-3-1-54-03. Available at <http://www.nc.ee/?id=11&indeks=0,3,159,1213&tekst=RK/3-3-1-54-03> (12.06.2008) (in Estonian).

human health and well-being but also those related to the objective value of the environment as such (here the “park as such”).

In the *Koidu Park* case^{*27}, the Tallinn district court dealt with a situation similar to that addressed in *Jämejala Park*. The case concerned an old and well-preserved park in Tallinn. Koidu Park was regularly used by local residents for recreational purposes. Local inhabitants filed a claim with the administrative court, seeking annulment of the proposal to change the local land use plan in a manner allowing erection of residential buildings in the park and, thereby, destruction of the park. The court here directly referred to principle 4 of the Rio Declaration and, erroneously, to Article 6 of the EC Treaty and ruled that the contested plan infringed on the integration principle and that this principle must be implemented not only when new legislation is prepared and adopted but also in administrative practice.

3.4. Governmental institutions taking care of integration

One cannot find special procedures of environmental integration in the Estonian legislative process. However, the Estonian Ministry of the Environment can and should take care of integration of environmental concerns in the framework of general procedures of legal drafting in Estonia. The legislation is usually drafted in ministries or other governmental bodies, before adoption drafts are sent to all ministries for comments. Unfortunately, the Estonian Ministry of the Environment in practice has not used this tool actively enough to promote environmental aspects of different policies.

There are no general requirements as to inviting environmental agencies to comment on or co-operate in the rule-making and individual administrative actions by agencies more remotely concerned with the environment.^{*28} Such general procedures are not present in Estonia. Intervention of environmental agencies can occur merely in the framework of environmental impact assessment for projects or strategic environmental assessment of plans and programmes.

3.5. Implementation of Directive 2001/42/EC^{*29} — on strategic environmental impact assessment

One of the major instruments of environmental integration in EC law is Directive 2001/42/EC of the European Parliament and of the Council of 27 June 2001 on the assessment of the effects of certain plans and programmes on the environment. Environmental assessment is an important tool for integrating environmental considerations into the preparation and adoption of certain plans and programmes that are likely to have significant effects on the environment in the Member States, because it ensures that such effects of implementing plans and programmes are taken into account during their preparation and before their adoption.

Strategic environmental assessment (SEA) is the assessment of environmental effects of policies, plans, and programmes. The practice of SEA is closely related to environmental impact assessment (EIA), which is the evaluation of environmental effects of development projects. Strategic environmental assessment should strengthen EIA because it addresses potential environmental problems at a higher and earlier level in the development process and because it aims at integrating environmental requirements into decision-making.^{*30}

The key measure for transposition of the directive is the Environmental Impact Assessment and Environmental Management Act^{*31}, approved by Parliament on 22 February 2005. The first section of the act deals with assessment of the effects of certain public and private projects on the environment. The second major section of the act regulates the procedure of strategic environmental assessment and transposes Directive 2001/42/EC.

Section 22 of the previous EIA act (from 2000) stated that the potential environmental impact resulting from activities proposed by development plans or programmes had to be assessed in the course of drafting of the plan or programme.^{*32} The Planning Act contained similar provision concerning land use plans (in § 30). This meant that there was no specific procedure for environmental impact assessment for a plan and, accordingly, no procedural guarantees. In most cases, assessment of the environmental impact of plans was not carried out

²⁷ Tallinn District Court, 18.04.2008, 3-06-1136.

²⁸ By this we mean administrative agencies in charge of policies which *prima facie* do not impact on the environment but do so indirectly or upon deeper consideration.

²⁹ Council Directive 2001/42/EC of 27 June 2001 on the assessment of the effects of certain plans and programmes on the environment. — OJ L 197, 21.07.2001, pp. 30 – 37.

³⁰ S. Marsden, J. de Muller. Strategic Environmental Assessment and Sustainability in Europe — How Bright is the Future. — Review of European Community and International Environmental Law 2005 (14) 1, p. 50.

³¹ Keskkonnamõju hindamise ja keskkonnajuhtimissüsteemi seadus. Adopted on 22.02.2005. — RT I 2005, 15, 87 (in Estonian).

³² Keskkonnamõju hindamise ja keskkonnanäideteerimise seadus. Adopted on 14.06.2000. — RT I 2000, 54, 348 (in Estonian).

at all or at least was not conducted carefully enough. Impact assessment was 'hidden' in the general planning procedure.

Estonia has, in general, transposed Directive 2001/42/EC (including the annexes to it) properly; however, there are a number of deficiencies as well. The most important deficiencies are related to specification of the plans and programmes and detailed arrangements for consultations and dissemination of information.

The main conformity problems are as follows.

- Subsection 2 (2), litra a, first indent of the directive specifies which plans and programmes are subject to preparation **and/or** adoption by an authority at national, regional, or local level or are prepared by an authority for adoption, through a legislative procedure by Parliament or the government. According to Estonian law (§ 31 of the Environmental Impact Assessment and Environmental Management Act), a strategic environmental impact assessment is carried out only if the strategic planning document is established by a legal act of a parliament, government, national-level governmental body, or body of local government. Accordingly, the Estonian national law does not cover plans and programmes having potential environmental impact that are prepared but not established by a legal act. This should be considered a major mistake in transposition of the directive.
- Subsection 3 (6) requires that in the case-by-case examination and in specifying types of plans and programmes those authorities shall be consulted that, by reason of their specific environmental responsibilities, are likely to be concerned by the environmental effects of implementing said plans and programmes. Estonian law (§ 34 (4) of the Environmental Impact Assessment and Environmental Management Act) stipulates that opinion shall be sought at least from the Ministry of Social Affairs, the Ministry of Culture, and the Ministry of the Environment, as well as from the county environmental department or a local government body. It is obvious that the list of authorities cited as those that should be consulted is not exhaustive. Other authorities might be likely to be concerned by the environmental effects of a plan or programme — such as the environmental inspectorate (responsible for enforcement), the border guard department (responsible for marine pollution), and those responsible for administration of protected areas. If necessary, these authorities should be consulted as well. By contrast, Estonian law is ambiguous and stipulates that other authorities **may** be consulted. It is obvious that in this respect the discretion is too broad and Estonian law should be made more concrete.
- As far as specification of relevant plans and programmes is concerned, Estonian transposition is controversial. As was mentioned above, Estonian national law does not cover plans and programmes that could have an environmental impact and are prepared but not established by legal act. From this standpoint, the Estonian definition is narrower than the directive's definition. From another angle, the Estonian definition is broader. The scope of the directive covers only plans and programmes that are required by legislative, regulatory, or administrative provisions. This requirement is missing from Estonian law. Estonian law is stricter than the directive, as plans and programmes that are not directly required by legislative, regulatory, or administrative provisions are covered as well. The last argument, of course, has more theoretical relevance. I do not believe that the Estonian authorities are keen to adopt plans or programmes on a voluntary basis.

3.5.1. Assessment of SEA practice

Strategic environmental assessment is a relatively new instrument in Estonia, and specialist studies of its effectiveness are not available. However, two problems, which currently are under active discussion in Estonia, can be pointed out. Both of these issues are related to the interrelations of SEA and EIA.

Firstly, in many cases, plans or programmes subject to SEA are so general and include so many uncertainties that SEA seems to be quite pointless. In reality, this procedure is not capable of creating new knowledge about environment-related aspects of the plan, which have to be taken into account in decision-making.

Secondly, in many cases, the plan or programme subject to SEA is already detailed, enabling performance of full-scale environmental impact studies. In such cases, EIA for the planned project seems to be pointless.

In summary, the main problem is that impact assessment should be done at those stages of the procedure where there is enough information for prudent assessment, and unnecessary, lengthy, and costly parallel procedures should be avoided.

4. Conclusions

Integration has achieved the status of a general principle of EU law. Its main addressees at this level are Community institutions, but it is indirectly binding for Member States as well, insofar as they are implementing EU policies.

The integration principle covers not only definition and implementation of all policies having even remote impact on the environment but also individual activities. The principle is closely related to that of sustainability but is more demanding still, as it instructs those it addresses to achieve a certain environment-related material result — a high level of environmental protection. This means that the principle has not only a procedural dimension (e.g., with SEA) but a substantive element as well.

The integration principle does not merely enable relevant authorities to restrict economic activities if this is necessary for achieving a high level of protection; it also commands them to do so if this is necessary. At the same time, the integration principle leaves to the institution very broad room for discretion with respect to the kind of environmental requirements to integrate, and to what extent to do so. Similarly to the achievement of a high level of environmental protection, integration does not necessarily mean precedence over other policies.

The Estonian Constitution (in its §§ 5 and 53) and environmental framework legislation (the nation's Sustainable Development Act, Planning Act, and Nature Protection Act) contain indirect reference to the integration principle and can effectively facilitate internalisation of environmental concerns in other policy areas and relevant administrative practice.

The Estonian judiciary has interpreted the integration principle in the context of exercise of administrative discretion. Estonian courts have pointed out that environmental concerns should have significant legal weight and that they can and must compete on equal footing with economic and social concerns.

One of the most significant instruments of integration — the SEA directive — has been transposed into Estonian law correctly in general, but there are still important conformity problems as far as definition of plans and programmes and consultational requirements are concerned.



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The Compatibility of the Estonian Corporate Income Tax System with Community Law

The Estonian corporate income tax system (hereinafter ‘CIT system’), effective from 1 January 2000, has merited substantial interest from tax law scholars by virtue of its peculiarity and difference from traditional CIT systems. This article is intended to give an overview of the advantages and drawbacks of the Estonian CIT system and to examine the compatibility of this system with the relevant EC law.

The article starts with presentation of the background of the Estonian CIT reform in 2000 and the reasons for the reform. It demonstrates how beneficial the new CIT system is both for the state and for the taxpayers. Furthermore, the article focuses on the problems associated with the Estonian CIT system and provides analysis of the compatibility of the system with EC law, especially Directive 90/435/EEC on the common system of taxation applicable in the case of parent companies and subsidiaries in different Member States¹ (hereinafter referred to as ‘the Parent–Subsidiary Directive’). Also, the relevant European Court of Justice (ECJ) case law is examined. Thereafter, changes in the Estonian CIT system for 2009 are discussed. Finally, the article introduces the CIT reform of 2008 in Moldova, in which the country decided to make its CIT system similar to the Estonian one and describes the essay competition in Germany concerning deferred taxation.

¹ Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (OJ 1990, L 225, p. 6) with further amendments.

1. The background to the Estonian CIT reform of 2000

The version of the Income Tax Act (hereinafter: ITA) that took effect on 1 January 2000^{*2} was the third Income Tax Act in Estonia following the nation's regaining of its independence in 1991. Until 1 January 1994, personal income tax and corporate income tax were stipulated in two different acts. On 8 September 1993, the Estonian Parliament had passed a new Income Tax Act, which regulated both personal and corporate income tax; this took effect on 1 January 1994. However, this act had been amended 34 times since then, and some of these changes undermined the taxable base, rendered application of the Income Tax Act ineffective, and threatened to distort competition.^{*3} It was, therefore, necessary to draft a new Income Tax Act.

On 1 January 2000, the new Income Tax Act came into force that stipulated the unique CIT system of Estonia. The main difference of the Estonian CIT system from traditional systems is that profits are not subject to tax at the moment when they are earned. Instead, taxation is deferred until the distribution of profits. Additionally, expenses not related to business and, therefore, not deductible in traditional CIT systems are subject to tax in the Estonian CIT system. Consequently, the difference from the traditional expression of the system is only technical (the timing of tax liability); however, the Estonian CIT system is easier to comply with both for taxpayers and for the tax administration.^{*4}

The aim of the CIT reform of 2000 was to facilitate the development of enterprises and attract investors. This objective was undoubtedly achieved, as the profits of the companies have grown significantly.^{*5} Furthermore, because of the CIT reform, the unequal treatment of different legal persons was eliminated, since all tax incentives were abolished. As a result of the reform, there are no special rules favouring certain economic sectors, giving an incentive for investments in certain regions, or special tax incentives for foreign investors.

2. Advantages of the Estonian CIT system

The main merit of the Estonian CIT system is that it is simple and easy to both understand and administer, by virtue of its minimum number of exceptions and deferral of taxation of profits from the moment when they are earned till their distribution. Such a difference in timing enables preservation of all substantial elements of a traditional CIT system and at the same time to reduce considerably the number of technicalities from that required in a traditional CIT system.

Under a traditional system, in order to establish the taxable amount, the commercial profits are, first of all, calculated according to the accounting rules; then they are adjusted on the basis of the tax rules (e.g., certain expenses increase the taxable amount). In Estonia, distributed profits reflect the commercial profits and, additionally, non-deductible expenses are taxed on the cash basis. So, the only difference seems to be in timing; however, the Estonian CIT system has a considerable advantage — there is no need for amortisation and depreciation rules.

Moreover, since the Estonian Commercial Code^{*6} stipulates that profits can be distributed with the proviso that there are no losses from previous years (§ 276 of the Commercial Code), there is no need for special rules regulating carrying forward of losses. If the company has losses from previous years, the profits cannot be distributed and, therefore, are not subject to tax.

Additionally, the distributed profits and payments taxable on the corporate level are not subject to personal income tax on the level of the recipient. Therefore, double taxation is fully avoided. Furthermore, as natural persons do not have a liability to declare such payments, the number of tax returns submitted, as well as that of possible mistakes and corrections of tax returns, is reduced. Consequently, the administrative burden and compliance costs are also reduced. Because of these advantages, most corporate taxpayers are satisfied with the Estonian CIT system and would not like it to be changed.^{*7}

² Tulumaksuseadus. – RT I 1999, 101, 903; 2007, 44, 318 (in Estonian). English translation available at <http://www.just.ee/23295> (21.07.2008).

³ L. Lehis. Tulumaksuseadus. Kommenteeritud väljaanne (Income Tax Act. Commented edition). Tartu: OÜ Casus 2000, p. 10 (in Estonian).

⁴ See also A. Kurist, E. Uustalu. National Report (Estonia) for IFA Sydney Congress 2003 Subject I. – Trends in Company / Shareholder Taxation: Single or Double Taxation. Cahiers de droit fiscal international. Kluwer 2003, pp. 334–335.

⁵ Profits of the companies have grown from EEK 4 billion in 1999 to EEK 62 billion in 2006 and corporate tax revenues from EEK 1.6 billion in 1999 to EEK 3.5 billion in 2007 (Statistical Office of Estonia <http://www.stat.ee/statistics>).

⁶ Äriseadustik. – RT I 1995, 26–28, 355; 2008, 27, 177 (in Estonian). English translation available at <http://www.just.ee/23295> (21.07.2008).

⁷ P. Reiljan, K. Oja. Valitsuse otsus meeldib ettevõtjale (Government's decision pleases businessmen). – Äripäev, 6.07.2007 (in Estonian).

3. Problems associated with the Estonian CIT system

Discussion of the problems that might emerge from the Estonian CIT system as effective from 1 January 2000 arose long before the system was implemented. Most of the anticipated problems did not, however, occur, and those that did take place were promptly eliminated. This section of the paper provides an overview of the expected and actual problems associated with the Estonian CIT system and the way in which they were solved.

Before the new Income Tax Act was passed, one of the concerns was that Estonia would be regarded as an offshore tax haven. The reason for this was a mistaken understanding of the Estonian CIT system, which, unfortunately, still prevails to some extent among tax law scholars. According to this misunderstanding, the CIT rate is considered to be 0% and the distribution tax is said to exist in Estonia, which is not correct, as one can see on the basis of the description above.

Regardless, the Estonian tax system does not have any of the features distinctive of tax havens. Firstly, corporate profits are always subject to CIT upon distribution, and the tax rate is 21% in 2008 (to be 20% for 2009, 19% for 2010, and 18% as of 2011). Moreover, there are no isolated so-called 'ring fencing' regimes, and domestic and foreign income are treated equally in Estonia. All companies are liable to pay taxes and to render their accounts, and penalties are imposed on companies in breach of these liabilities. Additionally, the Estonian tax authorities exchange information concerning Estonian residents and income derived in Estonia. Finally, the ITA stipulates a number of anti-avoidance rules, concerning, for example, transfer pricing, controlled foreign company (CFC) rules, and taxation of hidden profit distribution.^{*8}

One more concern of those who mistakenly considered the Estonian CIT rate to be 0% was that Estonia might have problems with tax treaties, because the subject-to-tax condition is not fulfilled. Although the Estonian CIT rate was 26% in 2000 and, therefore, the subject-to-tax condition was met, problems arose with the double taxation treaty between Estonia and Latvia.^{*9} As a result, a new tax treaty was made applicable in this connection from 1 January 2002.^{*10} The main difference between the two treaties is that the newer treaty stipulates the limited right of the source state to tax dividends, interest, and royalties that were taxable only in the state of residence according to the previous treaty. Furthermore, the initial tax treaty enabled elimination of double taxation using both the credit and exemption method. The new tax treaty lays down only the credit method.

Originally, the ITA provided for tax-exemption of distributed profits if they were paid to resident companies with a view to eliminating double taxation. Profits distributed to non-residents were subject to tax. However, as the tax treaties contain a non-discrimination clause, the ITA was amended, and since 1 January 2003 the profits of companies have been taxed upon distribution without regard for the residence of the recipient. So, the problem of unequal treatment of residents and non-residents was solved, and currently the tax liability of a company distributing profits does not depend on the recipient.^{*11}

In dealing with problems associated with the Estonian CIT system, another of its posited drawbacks is worth mentioning. This disadvantage is that dividends do not constitute taxable income of natural persons. As a result, dividends are not included in the aggregate amount of all types of taxable income from which personal allowances are deducted. Therefore, if a natural person does not have any income apart from dividends, he or she cannot use personal allowances and deductions.^{*12} However, it seems to be reasonable that a person cannot deduct personal allowances if he or she does not have any taxable income and, consequently, tax liability does not arise.

If we compare the Estonian CIT system with CIT systems in other countries, it becomes clear that the Estonian system is advantageous for individual shareholders, as double taxation is not only mitigated but completely eliminated. There are two ways to provide full relief from economic double taxation: exempting dividends from taxation at shareholder level or at the company level.^{*13} Estonia applies the former exemption type, taxing corporate profits at the level of the company. As a result of the exemption, individual shareholders cannot deduct personal allowances from the dividend income, which is considered to be a disadvantage of the Estonian system. However, Estonia is not the only country where dividends are tax-exempt in the hands of the recipient. For example, Greece has applied a dividend exemption system since 1992. Under this system, corporate profits are taxed at the company level and dividends are not subject to further taxation at shareholder level. Therefore, natural persons cannot deduct personal allowances if they have only dividend income.^{*14}

⁸ L. Lehis (Note 3), pp. 16–17.

⁹ Eesti Vabariigi ja Läti Vabariigi vaheline tulu- ja kapitalmaksuga topeltmaksustamise vältimise ning maksudest hoidumise tõkestamise leping (Convention between the Government of the Republic of Estonia and the Government of the Republic of Latvia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income). – RT II 1993, 107 (in Estonian).

¹⁰ Convention between the Government of the Republic of Estonia and the Government of the Republic of Latvia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income. – RT II 2002, 33, 157.

¹¹ For more elaborated information regarding the dispute over the tax treaty see A. Kurist, E. Uustalu (Note 4), pp. 344–345.

¹² L. Lehis. *Maksuõigus* (Tax Law). Tallinn: Juura 2004, p. 256 (in Estonian).

¹³ P. J. Wattel, B. J. M. Terra. *European Tax Law*. 4th edition. Kluwer Deventer 2005, p. 263.

¹⁴ *Ibid.*, p. 264.

Mistakenly, some tax scholars are of the opinion that Estonia applies the second option for elimination of double taxation — providing exemption at the level of the company as Greece did until 1992.^{*15} However, the Estonian system is different from the system that Greece used to apply and resembles more the current Greek system, wherein corporate profits are taxed at the company level and dividends are tax-exempt at shareholder level.

It is said that in the case of the system that was employed in Greece and is by mistake attributed to Estonia, it is essential to apply a high withholding tax on profit distributions, both for domestic purposes with a view to preventing tax evasion by domestic shareholders not declaring the dividend received on their tax return and for international purposes, because if the recipient is not subject to domestic tax, the country of the company would receive no tax revenue.^{*16} In Estonia, there is no need for a withholding tax on profit distributions at all, since profits are taxed only once, at the company level. Consequently, there can be no tax evasion by domestic shareholders, as they are not liable to pay tax on dividends. Regarding the international purposes, Estonia receives the tax revenue despite the fact that the recipient is not subject to domestic tax, because resident companies are subject to corporate income tax. Thus, it is inaccurate to compare the Estonian CIT system to the Greek system effective till 1992, as Estonia provides relief from economic double taxation, exempting dividends at shareholder level. Therefore, the Estonian CIT system is to some extent comparable to the Greek system currently in effect, wherein the imputed disadvantage of the Estonian system is also present — an individual shareholder cannot deduct personal allowances from dividend income.

Additionally, such deductions are not possible under systems where a final withholding tax is applicable (e.g., optional in Portugal and under certain conditions in Italy)^{*17}, as well as in the case of half-rate systems. Under these systems, shareholders are in a more disadvantageous position than they would find in Estonia, as double taxation is not fully eliminated; it is only mitigated. For final withholding tax, corporate profits are taxed at the company level, and afterwards the tax is withheld from dividends and natural persons cannot deduct personal allowances from dividend income. In a half-rate system, corporate profits are taxed at the company level, income tax is withheld from dividends, and then dividends are taxed at half the marginal rate for other income and the tax withheld is credited against the final tax liability. Personal allowances are generally not deductible from dividend income.

Deductibility of personal allowances from dividend income is usually possible in half-base systems. However, it does not make these systems more advantageous, since they do not provide full relief from double taxation. In the case of half-base systems, corporate profits are taxed at the company level, then income tax is withheld from dividends, 50% or 60% of the dividend income is added to the aggregate income of the natural persons, personal allowances are deducted from the aggregate income, and the tax withheld is credited against the final tax liability. Despite personal allowances being taken into account, half-base systems eliminate double taxation only partially and, therefore, result in a less advantageous position of natural persons than the Estonian system provides.

The following table demonstrates the overall tax liabilities on dividends under different CIT systems.

	Estonian CIT system	Final withholding tax	Half-base system	Half-rate system
Corporate profit	100,000	100,000	100,000	100,000
CIT (20%)	20,000 (tax liability deferred till distribution)	20,000	20,000	20,000
Dividend	80,000	80,000	80,000	80,000
Withholding tax (10%)	—	8,000	8,000	8,000
Income subject to personal income tax	0	0	40,000	80,000
Deduction of annual personal allowance (30,000)	—	—	40,000–30,000 = 10,000	—
Personal income tax (20%)	—	—	2,000	8,000 (10% rate)
Credit for withholding tax	—	—	8,000	8,000
Remainder payable	—	—	0	0
Refunded	—	—	6,000	0
Shareholder's net income	80,000	72,000	78,000	72,000
Total tax levied	20,000	28,000	22,000	28,000

¹⁵ *Ibid.*

¹⁶ *Ibid.*, pp. 263–264.

¹⁷ *Ibid.*, p. 262.

The above table makes it obvious that the Estonian CIT system is generally more advantageous for the individual shareholder than other systems, despite the fact that personal allowances are not deductible from dividend income.

As follows from the aforesaid, Estonia has promptly eliminated all of the problems associated with the new CIT system, and the supposed drawbacks of the Estonian CIT system appear to be less disadvantageous, on balance, than what is seen in traditional systems.

4. Compatibility with EC law

It is a settled principle in the case law of the European Court of Justice that, although direct taxation falls within the competence of the Member States, they must nonetheless exercise that competence consistently with Community law.¹⁸ It is, therefore, important to assess whether the Estonian CIT system is compatible with EC law. Since some harmonisation measures have been taken in the field of direct taxation, it is, first of all, necessary to examine the consistency of the Estonian CIT system with the directives. The most relevant directive in the present case is undoubtedly the Parent–Subsidiary Directive. Consequently, the analysis of the conformity with this directive will follow.

4.1. The Parent–Subsidiary Directive contrasted against the Estonian CIT system

According to the preamble of the Parent–Subsidiary Directive, its objective is to create within the Community conditions analogous to those of an internal market. As tax provisions applicable to parent companies and subsidiaries of different Member States are generally less advantageous than those applicable to parent companies and subsidiaries in the same Member State, the directive seeks to eliminate such disadvantages. Therefore, Article 5 of the Parent–Subsidiary Directive compels Member States to exempt dividends and other profit distributions paid by a subsidiary established in one Member State to its parent company in another Member State from withholding tax, with a view to eliminating double taxation of such income in EU intra-group situations.

The term ‘withholding tax’ is not defined in the Parent–Subsidiary Directive. However, the ECJ has interpreted the notion of withholding tax within the meaning of Article 5 of the Parent–Subsidiary Directive in numerous cases. One of the first judgments was *Athinaiki*¹⁹, wherein the ECJ ruled that a withholding tax within the meaning of the Parent–Subsidiary Directive is, in essence, any tax payable in the event of distribution of profits by a subsidiary to its parent company.

Because of the deferral of taxation of profits as described above, two taxes are paid in Estonia at the moment of profit distribution:

- 1) a corporate income tax levied on the corporate profits, while the tax liability is deferred till the distribution of profits (in such a case, the taxpayer is an Estonian company distributing profits);
- 2) a withholding tax²⁰ on dividends paid to non-residents whose shareholding in the company distributing dividends is less than 15% (the taxpayer is a non-resident company receiving the dividend).

It is clear that the latter is a withholding tax within the meaning of Article 5 of the Parent–Subsidiary Directive. However, as the amount is not withheld from dividends paid to parent companies, the directive is not applicable. The former tax is a corporate income tax within the meaning of Article 4 of the Parent–Subsidiary Directive. Logically, the same tax cannot constitute both corporate income tax within the meaning of Article 4 and withholding tax within the meaning of Article 5. It would also be bizarre if there were two withholding taxes from dividends. Moreover, it is commonly accepted in international tax law that a withholding tax is a tax on income imposed at source; i.e., a third party is charged with the task of deducting the tax from certain kinds of payments and remitting that amount to the government.²¹ Thus, in the case of a withholding tax, the company making the payment is obliged to remit the tax liability amount of the recipient of the payment to the tax authorities. Paying the Estonian corporate income tax, companies fulfil their own tax liability.

¹⁸ For example Case C-446/03, *Marks & Spencer*. – ECR 2005, I-10837, paragraph 29; Case C-196/04, *Cadbury Schweppes and Cadbury Schweppes Overseas*. – ECR 2006, I-7995, paragraph 40; and Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation*. – ECR 2006, I-11673, paragraph 36.

¹⁹ C-294/99, *Athinaiki Zithopiia*, ECR 2001, I-6797.

²⁰ A withholding tax on dividends paid to non-residents will be abolished as of 1 January 2009.

²¹ IBFD International Tax Glossary. 4th edition. IBFD Publications BV 2001.

However, the fact that taxation of corporate profits in Estonia is deferred until the moment of distribution was sufficient for the European Commission to consider the Estonian corporate income tax to be a withholding tax within the meaning of Article 5 of the Parent–Subsidiary Directive. The commission relied on the *Athinaiki* judgment cited above, although the Greek system contested in *Athinaiki* was different from the Estonian CIT system. As a result, when the Act of Accession^{*22} of Estonia to the EU was concluded, the commission was of the opinion that Estonia had to change its CIT system. Therefore, Estonia was given a transition period, running until 2009, to eliminate inconsistencies with the Parent–Subsidiary Directive. The provision of the Act of Accession that concerns the transitional period is as follows:

By way of derogation from Article 5 (1) of Directive 90/435/EEC, Estonia may, for as long as it charges income tax on distributed profits without taxing undistributed profits, and at the latest until 31 December 2008, continue to apply that tax to profits distributed by Estonian subsidiaries to their parent companies established in other Member States.^{*23}

Consequently, according to the Act of Accession, Estonia is prohibited to tax distributed profits since 2009 only in cases where such taxation is not compatible with Article 5 (1) of the Parent–Subsidiary Directive. If there is no derogation from the directive, there is nothing to prevent Estonia from deferring the tax liability till the distribution of profits.

4.2. The compatibility of the Estonian CIT system with the Parent–Subsidiary Directive

In order to judge whether or not the Estonian tax system is consistent with the Parent–Subsidiary Directive, it is important to examine the tax system as a whole, not only as regards a single aspect. Moreover, instead of comparing formal features, it is essential to ascertain the reasons for imposing them and the aims they pursue. It is, therefore, necessary to analyse whether the tax system is in line with the overall objective of the directive.

As mentioned above, the purpose of the Parent–Subsidiary Directive is to eliminate double taxation as well as disadvantageous treatment of cross-border dividends as compared to domestic dividends. In the case of a traditional CIT system, corporate profits are generally taxed when they are earned. Additionally, the tax is withheld when the subsidiary distributes profits to its parent company. Thus, economic double taxation arises. If the parent company is a resident of another state, this state has a right to tax the worldwide profits of its resident, including dividends received from the non-resident subsidiary. In domestic situations, double taxation is usually avoided in accordance with the national legislation. In cross-border situations, there are tax treaties stipulating the methods of avoidance of double taxation. However, not all of the Member States have concluded tax treaties with each other. It was, therefore, necessary to take additional measures to avoid double taxation at Community level.

It is for the above-mentioned reasons that the Parent–Subsidiary Directive compels the Member State of a subsidiary to exempt the profits the subsidiary distributes to its parent company from withholding tax. Equally, the directive obliges the state of the parent company either to refrain from taxing dividends received from another Member State or, if it subjects such profits to tax, to entitle the parent company to a tax credit in relation to tax paid not only by the subsidiary but also by any lower-tier subsidiary. As a result, the profits are only taxed once.

As for the Estonian CIT system, the profits of the subsidiary are taxed for the first time when they are distributed (i.e., taxation of corporate profits is deferred) and there is no further withholding tax from dividends distributed to a parent company, irrespective of the domicile of the parent company. Thus, the Estonian CIT system does not give rise to either double taxation or disadvantageous treatment of cross-border dividends as compared to domestic dividends. Consequently, the Estonian CIT system conforms to the objective of the Parent–Subsidiary Directive.

Hence, as one can infer from the aforesaid, there is no derogation from Article 5 (1) of the Parent–Subsidiary Directive in the case of the Estonian CIT system. The prohibition of withholding tax from dividends paid by a subsidiary to its parent company as stipulated in Article 5 (1) aims at avoiding double taxation. The Estonian corporate income tax is the only tax due on the subsidiary's profits; thus, it does not give rise to double taxation of distributed profits. The mere fact that the tax liability arises when the profits are distributed is not sufficient for considering the tax to be a withholding tax. Besides, if the taxpayer is a subsidiary and the corporate income tax levied on the subsidiary's profits constitutes the first taxation of such profits, this corporate

²² Act of Accession of the Czech Republic, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Slovenia and Slovakia (OJ 236, 23.09.2003).

²³ See Annex VI, chapter 7, section 2 of the Act of Accession.

income tax can in no way be regarded as a withholding tax. This statement is supported by recent judgments of the ECJ, which will be analysed in the following section.

4.3. The Estonian CIT system in the light of ECJ cases

The European Court of Justice has interpreted the term ‘withholding tax’ within the meaning of Article 5 (1) of the Parent–Subsidiary Directive in a number of cases. The most important among these are *Athinaiki*, cited above, and *FII Group Litigation*.²⁴ Additionally, the ECJ assessed the scope of the Parent–Subsidiary Directive in the recent cases *Oy AA*²⁵ and *Burda GmbH*.²⁶ Below is examination of these ECJ judgments.

4.3.1. Case C-294/99, *Athinaiki*

Athinaiki provided the rationale for the commission’s opinion that the Estonian corporate income tax could constitute a withholding tax within the meaning of Article 5 (1) of the Parent–Subsidiary Directive. In order to determine how the commission has drawn such a conclusion from this case and whether or not it is reasoned well, scrutiny of the judgment follows.

The *Athinaiki* case concerned a dispute over taxation of profits distributed by a Greek subsidiary to its parent company situated in the Netherlands. According to the Greek CIT system contested in *Athinaiki*, the profits were taxed when earned; however, certain income was tax-exempt or subject to special taxation entailing extinction of tax liability. When a subsidiary distributed profits to its parent company and these profits included income that was tax-exempt or subject to special taxation, such income was taken into account in determination of the taxable profits of the subsidiary.

In assessing whether the Greek legislation is compatible with the Parent–Subsidiary Directive, the ECJ highlighted two factors that in its opinion were distinctive of a withholding tax:

- 1) the chargeable event for the taxation at issue was the payment of dividends;
- 2) the amount of tax was directly related to the amount of the distribution.²⁷

Additionally, decisive seems to be the fact that the increase in the basic taxable amount generated by the distribution of profits could not be offset by the subsidiary using negative income from previous tax years, contrary to the fiscal principle enabling losses to be carried forward that was nevertheless laid down in Greek law.²⁸ Therefore, the Greek tax disputed in the *Athinaiki* case could not be regarded as a corporate income tax, because the Greek legislation allowed offsetting losses from previous years for corporate income tax purposes. Conversely, there was no possibility of offsetting losses from the taxable amount generated by the distribution of profits. As a result, the ECJ considered the contested tax to be a withholding tax.

In order to determine the applicability of the *Athinaiki* judgment to the Estonian CIT system, it is necessary to analyse whether the Greek and Estonian systems are comparable. Indeed, the chargeable event for the Estonian corporate income tax is the distribution of profits and the amount of tax payable is in certain cases related to the amount of the distribution.²⁹ However, if the Estonian subsidiary has received dividends, it can apply either the exemption or credit method, depending on the size of the shareholding in the company distributing dividends. The credit method is also applicable in respect of interest and royalties received, if they meet certain conditions. As a result of application of the exemption or credit method, the taxable profit distributions or the tax on distributed profits is reduced. Consequently, the amount of tax payable is not related to the distribution’s amount if the subsidiary distributing profits has received dividends, interest, or royalties that meet certain conditions and have already been taxed.

That the Estonian subsidiary can deduct from the corporate income tax due on distributed profits the tax withheld from dividends, interest, or royalties received by the subsidiary is convincing evidence that the Estonian corporate income tax does not constitute a withholding tax. Otherwise, it would be quite unusual if it were possible to deduct the tax withheld from dividends, interest, or royalties received by the Estonian subsidiary from the tax withheld from dividends paid by this subsidiary.

One further crucial difference is that in Greece there was a corporate income tax and, additionally, tax on distributed profits in certain cases. In Estonia there is only corporate income tax, without any further distribution taxes.

²⁴ Case C-446/04, *Test Claimants in the FII Group Litigation*. – ECR 2006, I-11753.

²⁵ Case C-231/05, *Oy AA*.

²⁶ Case C-284/06, *Burda GmbH*.

²⁷ See paragraph 28 of the *Athinaiki* judgment.

²⁸ See paragraph 29 of the *Athinaiki* judgment.

²⁹ See chapter “Changes in the Estonian CIT System 2009” below about the amendments which will basically extinguish these aspects of the Estonian CIT system in order to highlight the compatibility with the Parent–Subsidiary Directive.

Moreover, the Greek legislation stipulated the right to carry forward losses from previous years, but only in cases of corporate income tax and not for tax due on distributed profits. As the rules of imposing of these two taxes differed, the tax on distributed profits could not constitute a corporate income tax. Contrarily, in Estonia, by virtue of deferral of tax liability until distribution of profits, there is no need for special rules regulating loss carry-forward. Specifically, the Estonian Commercial Code provides that profits cannot be distributed if the company has losses from previous years. As a result, tax liability cannot arise if the company has a negative income from previous years. Consequently, the Estonian CIT system is not comparable to the Greek one.

The issue of carrying forward loss seems to have ultimately contributed to the ECJ's final decision to a large extent. If the Greek legislation had avoided the situation where tax liability arises despite the existence of losses from previous tax years, the ECJ would most probably have come to the opposite conclusion. Therefore, account should be taken of the differences between the Greek and Estonian system before conclusions are drawn about the Estonian corporate income tax on the basis of the judgment dealing with the Greek CIT system.

4.3.2. Case C-446/04, *FII Group Litigation*

In the *Athinaiki* judgment, examined above, the ECJ diverged from the meaning of the term 'withholding tax' that was commonly accepted in international tax law. Generally, a withholding tax used to be viewed as a tax withheld and transferred to the tax authorities by the payer while the actual taxpayer is the beneficiary of the payment; thereafter, the tax withheld is credited against the recipient's final tax liability when the tax return is filed (with the exception of the final withholding tax). In a number of judgments³⁰ defining the concept of a withholding tax within the meaning of Article 5 (1) of the Parent–Subsidiary Directive, the ECJ nonetheless returned to this common interpretation of a withholding tax. Below, the meaning of a withholding tax in the light of these judgments is analysed on the basis of the ultimate case *FII Group Litigation*.

In the *FII Group Litigation* judgment, the ECJ has set forth the conditions that should be met in order for a tax to be considered a withholding tax. The ECJ held that it is a matter of established case law that a withholding tax is any tax on income received in the state in which dividends are distributed where

- 1) the chargeable event for the tax is the payment of dividends or of any other income from shares,
- 2) the taxable amount is the income from those shares, and
- 3) the taxable person is the holder of the shares.³¹

From the Estonian perspective, the most significant is the third condition, that the taxable person shall be the recipient of the dividends. Under the Estonian CIT system, the taxpayer is the Estonian subsidiary distributing profits to the parent company and the latter is not liable for paying income tax on dividends received.

The definition of a withholding tax in the *FII Group Litigation* case is followed by the reference to, inter alia, the *Athinaiki* judgment, wherein the ECJ has interpreted the term 'withholding tax' somewhat differently. One can, therefore, infer that the ECJ has considered all of the previous judgments where the term 'withholding tax' within the meaning of the Parent–Subsidiary Directive was interpreted and has drawn a general conclusion as to how the concept of withholding tax shall be defined henceforth. According to this definition, the Estonian corporate income tax is not a withholding tax, as the condition that the taxpayer shall be the recipient of the dividend is not fulfilled.

4.3.3. Case C-231/05, *Oy AA*

In addition to the cases in which the term 'withholding tax' is interpreted, there is an ECJ judgment wherein an attempt is made to ascertain the scope of the Parent–Subsidiary Directive. Below is the conclusion of the ECJ in the *Oy AA* judgment and assessment of its meaning for Estonia.

In the *Oy AA* case, the ECJ held that Directive 90/435 does not constitute the first taxation of income arising from a business activity of a subsidiary. Thus, the directive could not be a basis for supplying an answer to the question referred to the court.³²

Having explicitly ruled that the Parent–Subsidiary Directive does not regulate the first taxation of a subsidiary's profits, the ECJ has eliminated all doubts concerning the compatibility of the Estonian CIT system with the directive. The Estonian corporate income tax constitutes the first taxation of the subsidiary's profits, despite being levied only when the profits are distributed. No other tax is levied on the subsidiary's profits before the corporate income tax. Consequently, the Estonian corporate income tax cannot be in breach of Article 5 (1) of the Parent–Subsidiary Directive.

³⁰ Case C-375/98, *Epson Europe*. – ECR 2000, I-4243; Case C-58/01, *Océ Van der Grinten*. – ECR 2003, I-9809; Case C-446/04, *Test Claimants in the FII Group Litigation*. – ECR 2006, I-11753.

³¹ See paragraph 108 of the *FII Group Litigation* judgment.

³² See paragraph 27 of the *Oy AA* judgment.

4.3.4. Case C-284/06, *Burda GmbH*

Finally, on 26 June 2008, a decision was issued that clarified that in interpretation of the term ‘withholding tax’ all three conditions mentioned above, including the requirement that the taxable person be the holder of the shares — as stated in previous case law — must be met³³. Consequently, the court concluded that “a provision of national law which, in relation to cases where profits are distributed by a subsidiary to its parent company, provides for the taxation of income and asset increases of the subsidiary which would not have been taxed if they had remained with subsidiary and had not been distributed to parent company does not constitute withholding tax within the meaning of Article 5(1) of Council Directive 90/435”.³⁴ By stating this, the court took an opposite view to what had been concluded in the *Athinaiki* judgment³⁵ and thus indirectly also confirmed the compatibility of the Estonian income tax system with the directive.

5. Changes in the Estonian CIT system from 2009

Despite the evidence that in the case of the Estonian CIT system, there is no derogation from Article 5 (1) of the Parent–Subsidiary Directive, but before ECJ case on *Burda* was issued, Estonia took action in order to minimise the possible risks that the Estonian corporate income tax would still be deemed to be a withholding tax. Therefore, on 26 March 2008, Estonia adopted amendments to the income tax law³⁶ to change the corporate income tax system as of 1 January 2009 in order to highlight the compatibility with the Parent–Subsidiary Directive.

The spring 2008 amendments were meant to retain the distinctive feature of the Estonian corporate tax system — deferral of corporate income tax liability until the distribution of profits. The amendments provided for a change of the taxable period from calendar month to calendar year where the filing of the tax return and tax payment would have become due within six months after the end of the tax year. Additionally, the tax base would have been changed to comprise corporate profits distributed in the tax period adjusted by taxable gifts, donations, representation costs, expenses and payments unrelated to business. Furthermore, the taxable base would have been expanded by liquidation proceeds and payments made in the case of a reduction in the share capital of the company or redemption or return of shares in the amount by which they exceed monetary and non-monetary contributions to the equity of the company.

The annual corporate tax liability would have been complemented by advance payments due twice per tax period, with the amount of the instalments determined on the basis of the average taxable amount for the last three tax years and the tax rate currently in effect. When the tax return was filed and the corporate income tax due calculated, the advance payments would have been offset against the final tax liability. As a result of the amendments, none of the features distinctive of a withholding tax pursuant to the ECJ case law would have been present in the Estonian CIT system. The chargeable event would not have been the payment of dividends, and the taxable amount would have not been directly related to the amount of the distribution. Moreover, companies would have been liable to make advance payments of corporate income tax that is credited against the final tax liability on the joint tax base calculated in the tax return once a year. It is clear that there can be no advance payment of a withholding tax, especially if the instalments are determined on the basis of previous tax years instead of the payments made in the current tax year. Therefore, the Estonian corporate income tax should have not been constituting a withholding tax within the meaning of the Parent–Subsidiary Directive.

However, after the ECJ case on *Burda* was issued, it became clear that there is actually no need to change the Estonian corporate tax system as of 1 January 2009 to bring it in line with the Parent–Subsidiary Directive. Therefore, on 20 November 2008, new corporate tax law amendments³⁷ were adopted by the Parliament that abolished the amendments adopted earlier in spring. Thus corporate tax period remained a calendar month and no advance corporate tax payments were introduced.

In fact, the autumn law abolished as of 1 January 2009 the only real withholding tax that existed upon dividend payments, namely on those made to non-resident corporate portfolio shareholders. This amendment, however, was not related to the compatibility of the tax system with the Parent–Subsidiary directive, but was based on Commission’s infringement procedure of 31.01.2008³⁸ where the issue was raised whether the Estonian tax withheld from foreign pension funds is compatible with fundamental freedoms provided by the EC Treaty, when no similar tax is withheld on payments made to domestic pension funds.

³³ See paragraphs 61–62 of the *Burda* judgment.

³⁴ See paragraph 64 of the *Burda* judgment.

³⁵ Compare paragraph 64 of the *Burda* judgment and paragraph 55 of the *Athinaiki* judgment.

³⁶ Tulumaksuseadus. – RT I 2008, 17, 119 (in Estonian).

³⁷ Available at www.riigikogu.ee (draft 352 SE III). Law has not been published in State Gazette yet.

³⁸ European Commission’s press release IP/08/143.

6. The Estonian CIT system — only for Estonia or a good idea for others?

Estonia is the first country to establish a CIT system under which taxation of corporate profits is deferred until their distribution. Having created such a unique system, Estonia has attracted the attention of tax scholars all over the world. Moldova even decided to implement a CIT system similar to the Estonian one as of 1 January 2008. Furthermore, the German foundation *Humanistische Stiftung* (the Humanist Foundation) has conducted an essay competition regarding deferred taxation of corporate profits.

6.1. The CIT Reform of 2008 in Moldova

Moldova decided to make its CIT system similar to the Estonian system as of 1 January 2008; however, because of the inaccurate understanding of the substance of the Estonian CIT system, the new Moldovan system turned out to be different from the Estonian one.^{*39}

As a result of the CIT reform in Moldova, from 1 January 2008, the corporate income tax rate is reduced to zero and dividends distributed to resident corporate shareholders are subject to neither corporate income tax nor withholding tax. Dividends distributed to resident individuals are taxable at shareholder level at the general rates. As for dividends paid to non-resident shareholders, a final withholding tax is imposed on the gross amount at the rate of 15%, unless a tax treaty provides otherwise.^{*40}

Thus, corporate profits of Moldovan companies are not subject to tax at all from 1 January 2008, whereas in Estonia the tax liability of the companies is deferred until the distribution of profits. Being exempted from CIT, the Moldovan companies still have to withhold income tax at a rate of 15% from certain payments made to natural persons. Such a withholding tax constitutes a tax liability of the natural person receiving the payment, not of the company making the payment.^{*41}

It follows from the above that the only similarity between the Estonian and Moldovan CIT systems is that the retained profits of the companies are tax-exempt. However, in Estonia, corporate profits are subject to corporate income tax when they are distributed. Additionally, expenses that usually are not deductible under traditional systems are taxable in Estonia. Contrarily, corporate income tax has been abolished completely in Moldova.

Absence of corporate income tax may result in some of the problems that were discussed when Estonia decided to change its CIT system. For instance, problems may arise in relation to tax treaties, because the subject-to-tax condition is not fulfilled if there is no corporate income tax and double taxation does not take place. Consequently, contracting states do not have to refrain from taxation, as there is no need to avoid double taxation. Hence, Moldova would appear to have abolished corporate income tax in favour of it being levied by other states. Conversely, companies would not benefit from the new tax system. Moreover, some states might apply CFC rules in respect of Moldova.

These problems did not arise in Estonia, because corporate income tax was not abolished; the tax liability was simply deferred. However, there is a risk that such problems may be seen in Moldova, as corporate income tax has actually been abolished. Accordingly, it might be reasonable for Moldova to amend its system in order to make it more similar to the Estonian CIT system, with a view to avoiding the above-mentioned problems.

6.2. The essay competition in Germany concerning deferred taxation

Humanistische Stiftung, whose main objective is to promote modernisation of German income tax laws, has arranged an essay competition on the following topics:

1. When deferred taxation is applied to corporate profits, do the basic liberties set forth in the EC and EU treaties prohibit member states of the European Union from securing the taxation of income earned domestically?
2. Can deferred taxation provide a uniform measure for assessing the taxation of corporate profits in the European Union?

³⁹ А. Канду, С. Чебан. Налоговая конференция: вопросы для обсуждения. — Экономическое обозрение, 19.10.2007, No. 38, p. 18. E. Banaru. Moldova kak novoe privilekatelnoe napravlenie na investitsionnoi karte Evropii. — BusinessClass 2008/1, pp. 64–67.

⁴⁰ Global Tax Surveys, Chapter on Moldova. Available at www.ibfd.org.

⁴¹ А. Канду, С. Чебан (Note 39), p. 18.

The current German tax system is considered to be one of the reasons for the ailing condition of the German economy, and *Humanistische Stiftung* finds it necessary therefore to change the system. One of the alternatives to the current German tax system is a system of so-called deferred taxation. There are a number of advantages to deferred taxation, which *Humanistische Stiftung* has brought out.

Firstly, whereas traditional systems obstruct growth and employment, deferred taxation facilitates innovativeness and promotes development and employment. Moreover, deferred taxation does not lead to a shifting of the tax burden from income derived from business to income from labour. In addition, it does not result in definitive shortfalls in tax revenue; it gives rise to tax deferrals without actual loss of tax revenue. In addition to fostering growth, employment, and positive influence on equity capital in companies, deferred corporate taxation provides equal treatment of all forms of business entities and offers great simplicity. Hence, *Humanistische Stiftung* has concluded that it seems to be feasible to apply distribution of profits as a starting point for taxation in all Member States.^{*42}

7. Conclusions

As has been demonstrated, while being different from traditional systems on account of its deferral of taxation until profit distribution, the Estonian CIT system maintains all of the fundamental elements of a traditional CIT system and at the same time minimises the number of technicalities essential in a CIT system. As a result, the Estonian CIT system is simple and transparent, fosters investments, and mitigates companies' motivation to hide profits. By comparison with traditional systems, one can observe that the Estonian CIT system is easier to comply with for both the taxpayer and those in tax administration.

It is fundamental, however, not to confuse the tax deferral provided under the Estonian CIT system with the tax-exemption of profits at corporate level that is mistakenly attributed to the Estonian system. The tax liability is merely deferred in Estonia, and distributed profits are tax-exempt at the shareholder level, not at the level of the company distributing profits.

Additionally, it should be stressed that, since the Estonian CIT system is in line with the objective of the Parent–Subsidiary Directive, the mere fact that taxation is related to the distribution of profits does not necessarily mean that corporate income tax constitutes a withholding tax within the meaning of the language of the directive. Therefore, instead of drawing conclusions on the basis of formality, one should examine the substance of the Estonian CIT system. Such an assessment clearly shows that there is no breach of the Parent–Subsidiary Directive and that, being a primary tax levied on corporate profits, the Estonian tax constitutes a corporate income tax, not a withholding tax. This viewpoint is supported by the recent judgments of the ECJ.

Moreover, changes of the Estonian CIT system for 2009 highlight the fact that the system is compatible with the Parent–Subsidiary Directive. As a result of these amendments, the chargeable event will no longer be the payment of dividends as such, and the taxable amount will not be directly related to the amount of the distribution. Additionally, the new liability to make advance payments of corporate income tax on the basis of the average taxable amount for the last three tax years, which will be credited against the ultimate tax liability, will make it more clear that the Estonian corporate income tax is not a withholding tax, since there can be no advance payment of a withholding tax.

Finally, the interest shown by tax scholars in the Estonian CIT system and the experience of Moldova and Germany in relation to the system of deferred taxation show that other states could benefit as well from the implementation of such a CIT system. Furthermore, as the German foundation *Humanistische Stiftung* has pointed out, deferred taxation seems to be feasible for providing a uniform means of assessing taxation of corporate profits in the European Union.

⁴² Available at <http://www.humanistische-stiftung.de/auslobung-2/de/>.



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The Impact of European Union Law on Employee Involvement in Estonia

1. Introduction

Estonia started to co-ordinate its labour legislation with European Union (EU) law after entering into the Association Agreement^{*1} with the European Communities and their Member States in 1995, insofar as with that agreement Estonia undertook to converge and harmonise Estonian legislation with European Union law, especially in the fields of commerce, economy, and related areas, including with respect to matters pertaining to employee protection (addressed in Articles 68 and 69 of the Association Agreement). According to the European Commission White Paper of 1994, the associated Member States had to implement the necessary accession measures in order to transpose into national law and practice the basic rules of Community social policy, including the seven labour rights directives established by that time.^{*2} Of this legislation, employee involvement was discussed in Directive 94/45/EEC^{*3}, on the establishment of a European Works Council, and the obligation to inform and consult employees was also included in Directive 75/129/EEC^{*4}, on collective redundancies, and in Directive 77/187/EEC^{*5}, on transfers of undertakings.

The labour legislation that existed in Estonia before accession to the EU included no fundamental disagreement with EU law; in some areas that the EU had considered necessary to regulate, however, rules had not been established or were insufficient in their detail.^{*6} Three areas can be pointed out in which the harmonisation

¹ Association Agreement between the European Communities and their Member States and the Republic of Estonia (Europe Agreement). – RT II 1995, 22–27, 120 (in Estonian).

² Valge raamat. Assotseerunud Kesk- ja Ida-Euroopa riikide ettevalmistamine integreerumiseks Euroopa Liidu siseturgu (White Paper. Preparation of the Associated Central and Eastern European Countries for Integration into European Union Internal Market). Tallinn: Eesti Õigusteabe Keskus 1996, pp. 81–94 (in Estonian).

³ Directive 94/45/EC on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees. – OJ L 254, 30.09.1994, pp. 64–72.

⁴ Directive 75/129/EEC on the approximation of the laws of the Member States relating to collective redundancies. – OJ L 48, 22.02.1975, pp. 29–30. This Directive has been replaced by Directive 98/59/EC which has the same title (OJ L 225, 12.08.1998, pp. 16–21).

⁵ Directive 77/187/EEC on the approximation of laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of businesses – OJ L 61, 5.03.1977, pp. 26–28. This Directive has been replaced with Directive 2001/23/EC which has the same title (OJ L 82, 22.03.2001, pp. 16–20).

⁶ On the harmonisation of Estonian labour legislation with EU law see M. Muda. Improving Estonian Labour Legislation on Integration with Europe. – *Juridica International* 1996, pp. 109–139; M. Muda. Application of International Labour Standards in the Regulation of Employment Relationship in Estonia. – *Juridica International* 1997 (2), pp. 112–118.

of Estonian legislation with European law turned out to be most problematic. These are the equal treatment of employees, the limitation of weekly maximum working time, and employee involvement.⁷ While with respect to harmonising the regulation of the amount of working time the most immediate necessity was to change practical organisation of work in order to decrease working time from 60 hours to 48 hours a week⁸, with respect to equal treatment of employees and employee involvement the differences existed more in principle. Estonian national law included individual provisions addressing both areas, but in practice their meaning was marginal. While, with regard to equal treatment of employees, the reason behind the minimal regulation could have been the society's meagre knowledge of equal treatment and equal opportunities⁹, the absence of employee involvement regulation was mostly due to the low importance of employee trustees in shaping employment relationships.¹⁰

Neither had attention been paid to improving national employee involvement rules in the EU integration action plans drafted in Estonia in the second half of the 1990s for the implementation of the rules established in the above-mentioned white paper.¹¹ On the one hand, this could be explained by the fact that the subject matter of employee involvement was unfamiliar to Estonian practice; on the other hand, also the EU started to pay more attention to developing this area only at the beginning of the current decade¹², when several significant employee-involvement-related directives were adopted — 2001/86/EC, on employee involvement in the affairs of the European Company (*Societas Europaea*, or SE)¹³; 2002/14/EC, establishing a general framework for informing and consulting employees¹⁴; 2003/72/EC, on the involvement of employees in a European co-operative society (or *Societas Cooperativa Europaea*, SCE)¹⁵; etc.

Although collective employment relationships have developed little in Estonia and consequently the associated employee involvement issues have been relatively unfamiliar, Estonia has now brought its labour legislation into concordance with the respective EU provisions. Hence, this article aims to examine the impact the transposition of EU employee involvement rules has had on the functioning of employment relationships in Estonia. In order to reach this goal, the author firstly studies the definition and subjects of employee involvement, insofar as the position of the latter has a great influence on the efficiency of employee involvement, continuing with the general framework of employee involvement, employee involvement in individual matters, and employee involvement in Community-scale undertakings, focusing not so much on analysing the transposition of directives verbatim as on trying to provide broader evaluation of the effects thereof.¹⁶

⁷ M. Muda. Impact of the European Community Labour Law on Estonian Labour Legislation. Labour Law in United Europe. 2003 m. spalio 16-18 d. Tarptautinės mokslinės konferencijos medžiaga. Vilnius, p. 93.

⁸ See also M. Muda. Trends in Regulating Working and Rest Time Estonia. Proceeding from the European Union Law – Juridica International 2000, pp. 147–148.

⁹ See M. Muda. Regulation of Gender Equality as a Fundamental Right in Estonia. – Juridica International 2002 (7), pp. 106–116.

¹⁰ See sub-item 2.2.

¹¹ M. Palmiste. Euroopa Liidu ja Eesti sotsiaalpoliitika diskursus (Socio-political Discourse of the European Union and Estonia). – Riigikogu Toimetised 2001 (4), p. 138 (in Estonian).

¹² Preparations for establishing the respective regulations were, however, started already in the 1970s. See R. Blanpain. European Labour Law. 11th and revised edition. The Hague: Kluwer Law International 2008, p. 713.

¹³ Directive 2001/86/EC supplementing the Statute for a European company with regard to the involvement of employees. – OJ L 294, 10.11.2001, pp. 22–32.

¹⁴ Directive 2002/14/EC establishing a general framework for informing and consulting employees in the European Community. – OJ L 80, 23.03.2002, pp. 29–34.

¹⁵ Directive 2003/72/EC supplementing the Statute for a European Cooperative Society with regard to the involvement of employees. – OJ L 207, 18.08.2003, pp. 25–36.

¹⁶ This article does not discuss employee involvement with regard to occupational health and safety issues, based on Directive 89/391/EEC on the introduction of measures to encourage improvements in the safety and health of workers at work (OJ L 183, 29.06.1989, pp. 1–8), insofar as the particularity and bulk of the regulation in that field deserves a separate study.

2. Definition and subjects of involvement

2.1. Definition of involvement

In the broadest sense, employee involvement means employee participation in making microeconomic decisions at the workplace (plant) or enterprise level.^{*17} Employee involvement thus refers to workers' opportunity to influence organisational decisions, regardless of their position in the company hierarchy.^{*18} Employee involvement can assume different forms. According to theoretical sources, employee involvement usually comprises the right to acquire information, the right to conduct consultations, and the right to co-decide (i.e., participate).^{*19} Also, EU employee involvement Directives 2001/86/EC (Article 2 (h)) and 2003/72/EC (Article 2 (h)) define employee involvement as any kind of procedure, including informing, consulting, and participation, that employee trustees can use to influence the decisions made in an undertaking.

Unlike several older Member States^{*20}, where the traditions of employee involvement go way back and where national regulations have served as a model in drafting the respective EU legislation, the concept of employee involvement was unfamiliar in the labour legislation existing in Estonia prior to accession to the EU. Influenced by EU law, the Trade Unions Act^{*21} (TUA) of 2000 obliged the employer to inform and consult the representatives elected by the trade union, but it did not elaborate on the concept of these terms, only listing the areas in which informing and consulting was obligatory.^{*22} The employee involvement-related terminology based on EU law is thus a new phenomenon in Estonia's legal order.

The concepts of informing and consulting employees have been established in the Employee Trustee Act^{*23} (ETA), which harmonises national law with EU Directive 2002/14/EC, and the Community-scale Involvement of Employees Act (CSIEA), which transposes into Estonian law Directives 94/45/EEC, 2001/86/EC, and 2003/72/EC, as well as the cross-border mergers directive (2005/56/EC).^{*24} Insofar as employees in Estonia do not have the right of co-decision — i.e., employees do not participate in the activity of the bodies of legal persons — the respective regulation is only laid down in the CSIEA, applying to European companies (SEs) and European co-operative societies (SCEs).

The concept of informing is laid down in the ETA's § 19 (1) and the CSIEA's § 3 (1) in almost identical wording^{*25} — informing refers to the informing of the employee trustees on an appropriate level that allows the employees to receive a clear and sufficiently detailed overview of the structure and economic and employment situation of the employer, on time, and possible development of the structure, situation, and other circumstances affecting the interests of employees, and to understand the effects of the situation and other circumstances on the employees. If one compares the definition of informing laid down in Estonian legislation to the corresponding definitions in the EU Directives (2001/86/EC (Article 2 (i)), 2002/14/EC (Article 2 (f)), and 2003/72/EC (Article 2 (i))), it may be concluded that, as the national regulation mostly provides a more thorough definition of the term than is required in EU law, it comprises that laid down in the directives.^{*26}

The ETA's § 19 (2) and CSIEA's § 3 (2) provide a similar definition of consulting — consulting means exchange of views and the establishment of dialogue between the employee trustee and the employer on an appropriate level allowing the employee trustee to express opinions and receive reasoned responses to the

¹⁷ M. Biagi, M. Tiraboschi. *Forms of Employee Representational Participation. Comparative Labour Law and Industrial Relations in Industrialized Market Economies*. R. Blanpain (ed.). 9th and revised edition. The Netherlands: Kluwer Law International 2007, p. 540. Employee involvement is also possible on the macro-economic level, but proceeding from EU directives underlying this article, only the company level is discussed here.

¹⁸ K. Jaakson, E. Kallaste. *Employee Participation: Case Study of Estonian Companies*. PRAXIS Center for Policy Studies 2005, p. 15. Available at http://www.praxis.ee/data/Employee_participation_2005_ENG.pdf (20.11.2008).

¹⁹ M. Biagi, M. Tiraboschi (Note 17), p. 505; K. Jaakson, E. Kallaste (Note 18), p. 15. In addition to these forms of involvement, employees can participate in a company's decision processes also through collective negotiations and collective labour disputes, but as the EU directives do not discuss these forms of involvement, neither does this article.

²⁰ The Member States of the EU prior to the enlargement of 1 May 2004 (EU15).

²¹ *Ametiühingute seadus*. Adopted on 14.06.2000. — RT I 2000, 57, 372; 2007, 2, 6 (in Estonian). The Act is available in English at <http://www.legaltext.ee/text/en/X30087K1.htm> (20.11.2008).

²² M. Muda. *Employee Involvement in Estonia*. — *Handbook of Employee Involvement in Europe*. M. Weiss, M. Seweryński (eds.). Kluwer Law International 2004, pp. 18–19.

²³ *Töötajate usaldusisiku seadus*. Adopted on 13.12.2006. — RT I 2007, 2 (in Estonian). The Act is available in English at <http://www.legaltext.ee/text/en/XX10005.htm> (20.11.2008).

²⁴ Directive 2005/56/EC on cross-border mergers of limited liability companies. — OJ L 310, 25.11.2005, pp. 1–9. As with regard to the organisation of employee involvement, Article 16 of this Directive largely refers to the provisions of Directive 2001/86/EC, it is not separately analysed in this article.

²⁵ The only difference is between the definition of employee trustees and employer.

²⁶ As the Directives specify the informing procedure, considering the level of its occurrence or its legal type, the respective rules have also been included in the ETA and the CSIEA.

opinions expressed from the employer. As Estonian legislation, similarly to Directives (94/45/EEC (Article 2 (f)), 2001/86/EC (Article 2 (j)), 2002/14/EC (Article 2 (g)), and 2003/72/EC (Article 2 (j)) open the definition of consulting by means of exchange of views, establishment of dialogue, and expressing of opinions, the definition of consulting provided in the national law is in compliance with EU law.

As the last form of employee involvement, employees' right of co-deciding (participating) was mentioned above. Under Estonian legislation, this is only possible with regard to SEs and SCEs.^{*27} Proceeding from Directives 2001/86/EC (Article 2 (k)) and 2003/72/EC (Article 2 (k)), the respective term is laid down in CSIEA § 46, where the participation of employees means the right to elect or appoint some of the members of the bodies of an SE or SCE, or the right to recommend or oppose the appointment of the members of the bodies of an SE or SCE. This, too, complies with the provisions of EU legislation.

In analysis of the definition of employee involvement, it may be concluded from the above that this concept was unfamiliar in Estonian law prior to EU accession and that it was adopted only as a consequence of the harmonisation of national law with EU regulations. Pursuant to Estonian law, employee involvement means informing, consulting, and participation of employees, and the respective terminology is in compliance with EU legislation. Insofar as the concept of employee involvement established in the legislation is clearly defined and sufficient, it creates a good legal basis for employee involvement in practice.

2.2. Subjects of involvement

The subjects of involvement constitute the employees through whom the employees' right to inform, consult, and co-decide is realised. A company's decision process usually involves the employee trustees or, in the absence of any such trustees, all employees. As different employee representation systems^{*28} have developed in EU member states historically, the employee-involvement-related directives discussed in this article do not interfere with the definitions thereof — pursuant to all of the relevant directives (94/45/EEC (Article 2 (d)), 2001/86/EC (Article 2 (e)), 2002/14/EC (Article 2 (e)), and 2003/72/EC (Article 2 (u))), employee trustees are considered to be the trustees of employees foreseen by national law and/or tradition. The present article further examines who constitutes employee trustees pursuant to Estonian legislation, and whether and how the respective regulation has been influenced by EU law.

As already mentioned, employees play a relatively insignificant role in shaping of employment and social relationships in Estonia. This is primarily due to the historical development of organisations representing employees. The first classic trade unions in Estonia were formed by the 1930s, but their activity was concluded by the occupation of Estonia by the Soviet Union in 1940. The aim of the trade unions operating in the Soviet era had to do with executing party policy rather more than with fighting for the rights and interests of employees. The restoration of traditional trade unions was only started in Estonia in 1990, meaning that employees have had only some 10 to 15 years to participate in the organisation of working life.^{*29}

The Employee Trustee Act of 1993 established the double-channel system of employee representation. This means that employees at a company could be represented either by a trustee elected by a trade union or by a trustee elected by a general meeting of employees not belonging to the trade union. In practice, however, the trustees were elected for those employers in relation to which a trade union had been formed^{*30} whose legal status and competence, including its role in informing and consulting employees, were specified in the TUA.

Insofar as employees' right of informing and consulting as established in Directive 2002/14/EC was intended to be ensured in Estonia by means of the trustees of employees, the new ETA drawn up for the transposition of that directive altered the system for electing employee trustees. In Estonia, the double-channel system of employee representation continued to be in force, but, in view of the fact that approximately 11% of employees belong to trade unions^{*31}, it was found that informing and consulting employees only through trustees elected by a trade union would not be sufficient for implementation of the directive. As noted in the explanatory note accompanying the ETA, a situation wherein the non-trade-union-members forming the overwhelming majority of employees would remain in electing their trustee not only deprived of the right to participate but also

²⁷ Also in the event of cross-border mergers of undertakings.

²⁸ According to research by Professor M. Biagi and Professor M. Tiraboschi, employee involvement may occur through a trade union, a representative body of employees independent from a trade union (e.g., a works council), a joint body of a trade union and a representative body of employees independent from the trade union, and a joint body of trustees of employees and employers. See M. Biagi, M. Tiraboschi (Note 17), p. 505.

²⁹ M. Muda (Note 22), pp. 7–11.

³⁰ See G. Tavits. Töötajate esindamine ettevõtetes ja käitistes – Eesti valikud (Representation of Employees in Enterprises and Plants — Estonia's Choices). – *Juridica* 2004/10, p. 698 (in Estonian).

³¹ Tööelu baromeeter 2005. Elanikkonna uuringu aruanne (Working Life Barometer 2005. Population Survey Report). Tallinn: Saar Poll OÜ 2006, p. 54 (in Estonian).

of any right to advise their 'representative' in his or her activity, ask him or her to report, and withdraw him or her, as appropriate, could in no event be considered right, just, and democratic.^{*32}

Proceeding from the above, a trustee of employees shall, according to ETA § 2 (1) of 2007, be elected by a general meeting of the employees, which may be called by a trade union operating at the employer, by the majority of the members of the trade union who are employed at the employer if the trade union has not been founded at the employer, or by at least ten per cent of the employees of the employer (see § 5 (1)).^{*33} The adoption of the ETA somewhat organises the system for representation of employees — with the enactment of the ETA, the main channels for employee representation are a trade union and a trustee elected by a general meeting of the employees — but the legal regulation of their competence continues to replicate the functions of the trade union and the trustee.^{*34}

In addition to the general framework of informing and consulting established in the ETA, and the respective rights of a trustee elected by a trade union, provided for in the TUA, the obligation of informing and consulting employees is in many cases (transfer of company, collective redundancy, application of employees with part-time work hours, and fixed-term employment contracts) also established in the Employment Contracts Act^{*35} (ECA). The employee trustees mentioned in the ECA do not constitute a category of independent trustees; for the individual matters mentioned, they also have to be either a trustee or a trustee elected by the trade union, as, pursuant to both ETA § 2 (2) and TUA § 14 (4), the latter are considered to be the employee trustees for the purpose of the ECA.

The ETA's §§ 19 and 21, and the corresponding rules of the ECA (in §§ 6³ and 89²), provide that in the absence of the employee trustees, the employer shall inform and consult the employees.^{*36} Such regulation can be considered justified, because in most Estonian companies the employee trustee has not been elected and thus the right to be involved must be ensured for all employees. It is, however, a matter of some question how the informing and consulting of all employees would occur in practice. Informing the employees is probably easier to accomplish, for example, by displaying the relevant information on a notice board or by means of electronic notification. But how can consultation with all employees be arranged? The employer has the possibility of obliging the employees to create a representation system as necessary for conducting consultations. In smaller undertakings, negotiations can be conducted also by means of a general meeting of employees. Another question regards ensuring the knowledge and skills of the employee trustees elected *ad hoc*, so that they could successfully protect their interests during the consultations.^{*37}

In addition to a trade union and trustee operating on the national level, a separate representation system was created in 2005 with the adoption of the CSIEA for involvement of employees in Community-scale legal persons. The CSIEA established a trustee elected by a general meeting of employees as the trustee of Estonian employees in the context of the regulation of European Works Council matters, SEs, and SCEs. This means that the members of a special negotiating body and a lawful European Works Council, as well as the members of a lawful representative body of employees in the case of SEs and SCEs, shall be elected from the companies and legal persons that are situated in Estonia at a general meeting of employees pursuant to the procedure of CSIEA § 17.^{*38}

Therefore, similarly to what is provided for by the ETA, employee trustees elected by a general meeting of employees shall participate in the process of employee involvement (or determination of the procedure thereof) also at the Community-scale level. In development of the regulation of the CSIEA (and of the ETA), the trade unions insisted that the prerogative of electing employee trustees must be given to trade unions, but this approach was discarded here, too, because of the relatively low membership of trade unions.^{*39}

³² Explanatory note to the Employee Trustee Act (5.06.2006), p. 6. Available at www.riigikogu.ee (20.11.2008) (in Estonian).

³³ As can be seen from this provision, trade unions play an important part in organising the general meeting of employees that elect the trustee. The establishment of such regulation was brought on by the great resistance of Estonian trade unions to changing the procedure for electing the trustee. By way of compromise, the ETA increased a trade union's possibilities of organising the election of a trustee, and specified the competence of the trustee elected by the trade union, provided for in the TUA.

³⁴ This means that the right to informing and consulting belongs to both the trustee, pursuant to ETA §§ 17–21, and the trade union, pursuant to TUA § 22, whereby the contents of informing and consulting overlap. Also both the trade union and the trustee have the right to represent the employees in conducting collective negotiations and in the resolution of collective labour disputes, the latter only if there is no trade union at the employer or no employees belonging to the trade union are working at the employer (TUA § 18 (1) 2), ETA § 9 (4), (5)).

³⁵ Eesti Vabariigi töölepingu seadus. Adopted on 15.04.1992. – RT 1992, 15/16, 241; 2007, 44, 316 (in Estonian). Available in English at <http://www.legaltext.ee/text/en/X1056K10.htm> (20.11.2008).

³⁶ The ECA nevertheless only foresees the obligation of informing (not consulting) all employees.

³⁷ M. Muda. Töölepingute kollektiivne lõpetamine (Collective Redundancies). – Juridica 2003/8, p. 556 (in Estonian).

³⁸ It is specified in CSIEA § 17 (2) that if several enterprises or legal persons are located in Estonia, the trustees of employees of which have to be determined, the general meeting of each enterprise or legal person shall elect three members to the joint representation, which, in turn shall elect the members of the appropriate body representing Estonia.

³⁹ Directive 94/45/EC. National Implementation Report. Estonia. Report elaborated by the workgroup lead by Merle Muda. Studies on the Implementation of Labour Law Directives in the Enlarged European Union. Labour Asociados Consultores 2007 (in possession of the author), pp. 3–4.

It can be concluded from the above that unlike the Member States belonging to the European Union at the time of drafting of the employee involvement directives, wherein an employee involvement mechanism of a clear structure and competence had been developed over the years, in Estonia a corresponding system is still being developed. While the enactment of the new ETA in 2007 specified the employee representation system to be applied in Estonia and employees may now be represented by trade unions and trustees elected by a general meeting of employees, the two channels of employee representation have not started to show clear-cut functioning. On the one hand, this may be on account of the thus far brief time in force of the ETA, making it difficult to assess the effects of this act just yet. On the other hand, the historical traditions of communication between Estonian employees and employers lead one to believe that the future will not bring a boom in the election of employee trustees either, and that the informing and consulting of employees will primarily be occurring in enterprises that have formed trade unions. At the same time it is questionable to what extent the trade union will have a say in these matters, because the overall world trends foresee the role of employee representation shifting increasingly from the trade unions to other representation channels.^{*40}

3. General framework of employee involvement

As mentioned before^{*41}, the general framework for informing and consulting employees is established by Directive 2002/14/EC on the EU level, and in Estonia the respective regulation is provided for in the ETA. The present article next will consider in which way the EU directive has been transposed into national legislation and what impact it has on the informing and consulting of employees in practice.

In creation of a general procedure for employee involvement, the first question for consideration is which employers should be subject to obligatory informing and consulting of employees. Pursuant to Article 3.1 of the directive, a Member State may choose whether to create an employee involvement system for employers employing at least 50 employees or, instead, at enterprises employing at least 20 employees. Pursuant to ETA § 17 (1), an employer who employs at least 30 employees is required to apply the informing and consulting procedure.^{*42} Estonian legislation thus establishes a lower threshold than is required by the directive. Insofar as upon establishment of such a threshold it was taken into consideration that the majority of Estonian employees work in micro- and small-sized enterprises, and that by establishing a higher threshold the directive would in its scope cover only a very insignificant proportion of employees^{*43}, the regulation of the ETA can be deemed to be justified and to act in favour of employee involvement.

Proceeding from Article 4.2 of Directive 2002/14/EC, the content of informing and consulting under the ETA is defined as follows: the structure of the employer, the staff, changes therein, planned decisions that significantly affect the structure of the employer and the staff, and planned decisions that bring about substantial changes concerning the organisation of work and employment contract relationships. In addition to the above-mentioned, the employer shall inform employees of the annual report details. Also the procedure for informing and consulting provided for in ETA § 21 (written provision of information in a manner enabling preparation for consultations, employees' right to present opinions and proposals, and also application to commence consultation with the purpose of reaching an agreement on the planned activity, etc.) complies with the provisions of the EU directive (Articles 4.3 and 4.4). The ETA thus provides a detailed employee involvement mechanism complying with the requirements of EU legislation, which should serve as a good basis for implementation of the informing and consulting of employees in practice.

The efficient functioning of the general framework of employee involvement is definitely supported by the trustee's obligation to maintain confidentiality of information, laid down in the ETA's § 11 on the basis of the regulation of Articles 6 and 7 of the EU directive, and by the protection of employee trustees ensured in the ECA in case of termination of contract by the employer.^{*44} The employer's liability in the event of failure to fulfil the obligation of informing or consulting or the event of submission of false information, as laid down in ETA § 24, is also of vital importance.^{*45}

⁴⁰ M. Biagi, M. Tiraboschi (Note 17), pp. 552–553; K. Jaakson, E. Kallaste (Note 18), p. 18.

⁴¹ See sub-item 2.1.

⁴² Pursuant to ETA § 18, the employer shall determine the number of employees upon approval of annual reports or when significant changes arise in the organisation of work, taking into account the six months' average number of employees as of the date on which the obligation of informing and consulting arises.

⁴³ Explanatory note to the Employee Trustee Act (Note 32), p. 8.

⁴⁴ Pursuant to the ECA, termination of employment contract of an employee is prohibited during representing the employee (§ 91 (1) 4)), and as a result of representation (§ 94 (3)); similarly, employment contracts with trustees of employees can be terminated during the term of authority of the employee and for within one year after termination of the authorisation only with the consent of the labour inspector (§ 94 (1)); trustees of employees have greater right of claim upon illegal termination of employment contract (§ 117 (3)), etc.

⁴⁵ Pursuant to the ETA, in the event of failure to perform the obligation of informing or consulting or submission of false information, the employer is punishable by a fine of up to 200 fine units. The same act, if committed by a legal person, is punishable by a fine of up to 50,000

It can be concluded from the above that the ETA regulation ensures that employees have the comprehensive right to be involved in the decision process of the employer. At the same time, we must recognise that, while the EU-level general framework of informing and consulting was created for the purpose of enhancing and improving the existing employee involvement mechanisms^{*46}, the Estonian ETA creates the respective system in an empty space.^{*47} In practice, therefore, Estonian employees and employers lack the habit of communicating with each other. Employee trustees have for the most part not been elected in Estonian enterprises. As explained above^{*48}, in the absence of employee trustees, the employer shall inform and consult all employees. It has, however, not been observed that the role of employees in making enterprise-related decisions has changed since the enactment of the ETA. The act may establish thorough employee involvement rules, but this does not mean that the informing and consulting of employees effectively occurs in practice.

4. Employee involvement in individual matters

Employee involvement in individual matters is seen as constituting the employer's obligation to inform and consult the employees with regard to significant reorganisations in the enterprise — i.e., transfer of enterprise and collective redundancy — and also the employer's obligation to inform employee trustees of use of non-typical forms of work — i.e., application of employees with part-time work hours and under fixed-term employment contracts. The informing and consulting of employees accompanying the reorganisation of the employer's activity has been laid down as an obligation in the above-mentioned directives 98/59/EC and 2001/23/EC. Informing the employee trustees of non-typical work forms has been mandated in the part-time work directive, 97/81/EC^{*49}, and in the fixed-term work directive, 1999/70/EC.^{*50} This section of the article discusses how the principles laid down in these EU directives have been transposed into Estonian legislation and whether the respective regulation establishes sufficient prerequisites for efficient involvement of employees.

As collective redundancy may bring about the redundancy of a large number of employees, the employer shall, pursuant to Article 2.2 of Directive 98/59/EC, conduct negotiations with the employee trustees before terminating the employment contracts of employees as to whether it would be possible to avoid or limit the termination of employment contracts and also on how to mitigate the consequences thereof. In order to provide substance for the consultations conducted with trustees of the employees, the employer is obliged to provide detailed information concerning the collective redundancy (see Article 2.3). In Estonia, the employee involvement regulation of Directive 98/59/EC has been transposed with the ECA's § 89², which complies with the provisions of EU legislation with respect to the purposes, content, and organisation of informing and consulting.^{*51}

As required in the directive (in Article 2.1), attempts are made to reach an agreement as a result of consultations conducted with employee trustees also pursuant to the provisions of the ECA. This constitutes a very strict form of consultations, which is similar to collective negotiations.^{*52} This provision grants the employee trustees relatively broad rights in making decisions related to the staff policy of the employer. This is also implied by the list of data that the employer is obliged to submit in writing to the employee trustees — employees can, among other matters, participate in determining the criteria for use in selection of dismissible employees and the methods for calculating the compensation for termination of an employment contract.^{*53} The ECA thus fully

kroons (3190 euros). Pursuant to § 47 of the Penal Code, a fine unit is the base amount of a fine and is equal to 60 kroons (3.80 euros). The value of 200 fine units thus amounts to 12,000 kroons (765 euros). See the Karistusseadustik (Penal Code). Adopted on 6 June 2001. — RT I 2001, 61, 364; 2008, 18, 87 (in Estonian). The Act is available in English at <http://www.legaltext.ee/text/en/X30068K7.htm> (20.11.2008).

⁴⁶ See A. C. Neal. Information and Consultation for Employees — Still Seeking the Philosopher's Stone? — Quality of Work and Employee Involvement in Europe. M. Biagi (ed.). The Hague/London/New York Kluwer Law International 2002, p. 83 ff.

⁴⁷ As explained in sub-item 2.1, prior to the enactment of the ETA, some provisions regarding the informing and consulting of employees were contained in the TUA. In certain cases (transfer of enterprise, collective redundancy, etc.), the employer's obligation to inform (and consult) the trustees of employees was also laid down in the ECA (see sub-item for further detail). The respective rules nevertheless did not reflect practice formed throughout times, but were established due to the necessity of transposing EU directives.

⁴⁸ See sub-item 2.2.

⁴⁹ Directive 97/81/EC concerning the Framework agreement on part-time work concluded by UNICE, CEEP and the ETUC. — OJ L 20.01.1998, pp. 9–14.

⁵⁰ Directive 1999/70/EC concerning the framework agreement on fixed-term work concluded by ETUC, UNICE, and CEEP. — OJ L 175, 10.07.1999, pp. 43–48.

⁵¹ If pursuant to Directive 98/59/EC the employer is obliged to inform and consult the trustees of employees, then pursuant to ECA § 89² the employer shall inform the trustees of employees and in their absence inform the employees, but the employer is subjected to the obligation of consulting only with regard to the trustees of employees.

⁵² R. Blanpain (Note 12), p. 598.

⁵³ M. Muda (Note 37), p. 557.

follows the ideas of Directive 98/59/EC and provides the employee trustees with a large-scale opportunity to intervene in the employer's decision process in the event of collective redundancy.^{*54}

Similarly to the collective redundancy, the transfer of an enterprise often entails significant staff-related reorganisations for both the transferor and acquirer of the enterprise. Pursuant to Article 7 of Directive 2001/23/EC, the former and the new employer shall therefore both inform the employee trustees (or, in the absence of such trustees, the employees) of the planned changes and have the obligation to conduct consultation in the event that, because of the transfer of enterprise, measures are implemented also with regard to employees (e.g., there is a need to reduce workforce). Although the aim of consultations conducted with employees is to reach an agreement, the directive only allows employees to participate in the enterprise's business-related decisions. It does not give them the right of veto.^{*55}

In Estonia the obligation of employee involvement in the event of transfer of enterprise is laid down in ECA § 6³, which appropriately transposes the requirements of Directive 2001/23/EC into Estonian law. As with collective redundancy, the ECA provides the employee trustees with the right to have an active say in the changes that are occurring (reduction of staff, structural reorganisation of the enterprise, adoption of new work methods and means, etc.) also in the event of transfer of enterprise. The ECA thus creates all of the relevant prerequisites for the involvement of employees, especially in the event that the transfer of enterprise brings with it changes affecting the situation of employees.^{*56}

Although statistics show that an average of 120 collective redundancies annually^{*57} occurred in the years 2003–2006^{*58} and that transfers of enterprises are not rare in practice either, no court actions regarding employee involvement have been brought in relation to these questions^{*59} and it seems that in the event of collective redundancies and transfer of enterprise the system for informing and consulting employees has been activated without problems. While the informing of employees is relatively easily arranged, conducting efficient consultations with employees requires good will and the existence of preliminary knowledge from the employer as well as the trustees of the employees. No surveys have been conducted in Estonia as to how the conducting of negotiations with employees in the event of collective redundancy and transfer of enterprise works in practice (what the content of the discussions is, what proposals employees usually make, to what extent employers consider the opinions of employees, etc.). Considering, however, the scant experience of employees and employers with intercommunication, one can conclude that such negotiations probably remain formal quite often.

With the establishment of Directive 97/81/EC, on part-time work, and Directive 1999/70/EC, on fixed-term work, in the late 1990s, the usage of respective non-typical forms of work in practice was recognised, with emphasis on avoiding discrimination against people in such employment relationships.^{*60} As both part-time and fixed-term workers have more superficial contact with the employer (enterprise), they often receive unjustifiably different treatment when compared to so-called typical employees. For the purpose of avoiding discrimination and monitoring the situation of employees with atypical work arrangements, directives 97/81/EC (clause 5.3 (e)) and 1999/70/EC (clause 7.3) oblige the employer to inform the bodies of employee trustees as to the use of such forms of work in the enterprise.

Attempts were made to include a similar principle in the Estonian ECA, but without success. Pursuant to the ECA, the employer shall notify the trustees of the employees of the opportunity for part-time work (§ 13¹ (2)) and fixed-term vacant jobs (§ 13² (2)). This kind of information should be of interest to employees themselves, rather more than their trustees. Although the trustees of employees do receive information on the usage of non-typical forms of work in an enterprise through the provision of such information, the establishment of such a requirement lacks purpose and the ECA regulation does not comply with the directives. At the same time, this cannot be considered an important violation of employees' rights, as only the content of

⁵⁴ If the employer fails to inform the employee trustees and consult with them pursuant to the ECA, the labour inspectorate as the competent authority shall not provide approval for the collective redundancy. The collective redundancy without approval of the labour inspectorate is, however, illegal. *Töölepingu seadus. – Tööõigus. Näidised ja kommentaarid. Äripäeva Käsiraamat* (Employment Contracts Act. – Labour Law. Examples and Comments. Äripäev handbook). Tallinn 2008; § 892 comm. 4.

⁵⁵ C. Barnard. *EC Employment Law*. 3rd edition. Oxford University Press 2006, p. 666.

⁵⁶ A shortcoming of the ECA can be deemed to constitute the failure to lay down the employer's liability in the event of violation of the rules of informing and consulting employees.

⁵⁷ Collective redundancies and compensation for collective redundancy. Five years of unemployment insurance in Estonia. 2002–2006. Estonian Unemployment Insurance Fund 2006, p. 32 (in Estonian). Collective redundancies are displayed in unemployment insurance statistics, because in that case the compensation for terminating employment contracts for employees is partly compensated by the Estonian Unemployment Insurance Fund.

⁵⁸ Provisions regarding the collective redundancies in the ECA entered into force on 1 January 2003.

⁵⁹ The employer's obligation to inform and consult with employees upon transfer of enterprise, laid down in the ECA, is in force as of 1 May 2004.

⁶⁰ C. Barnard (Note 55), pp. 469–471.

the information has been insufficiently prescribed; informing employees also comprises the realisation of the so-called passive involvement right.^{*61}

It may be concluded from the above that in Estonia a sufficient and appropriate employee involvement system has been created, enabling the employee trustees to participate in making decisions concerning the economic activities of an enterprise upon collective redundancy and transfer of enterprise as well as upon the usage of part-time and fixed-term employment contracts.^{*62} The procedure for informing employee trustees of the use of atypical forms of work requires some specification, but in practice this is not a problem in employee involvement. There are no statistical data concerning the informing and consulting of employees in respect of the above-mentioned questions. A survey conducted in 2005 on employee involvement shows, on the other hand, that, as a rule, employees do not participate in making strategic decisions regarding the economic activity of the enterprise.^{*63} This leads to the conclusion that the role of employees in co-deciding on the areas analysed in this section of the paper is not significant. Although the ECA regulation on informing and consulting employees had been in effect for only a short while at the time of the survey, presumably no significant changes have occurred in employee involvement in practice. As the reason behind the modest participation of employees cannot be inadequate legislation, the problem can also here probably be reduced to the awareness and competence of employees and employers.

5. Employee involvement with Community-scale legal persons

Involvement of employees in Community-scale legal persons is considered to refer to participation of employees in making decisions concerning the economic activities (including employees) of the employer in Community-scale undertakings and Community-scale groups of undertakings, also in SEs and SCEs, as provided for in the above-mentioned directives 94/45/EEC, 2001/86/EC, and 2003/72/EC. The main features of the regulation in these directives are similar — they first foresee the creation of a trustee body for employees (special negotiating body), then this body decides by agreement with the representatives of the legal person on the employee involvement mechanism to use, and eventually the rules for establishing a lawful representative body are laid down.^{*64} As a difference it can be pointed out that while in Community-scale undertakings and Community-scale groups of undertakings the trustees of employees must only have a guaranteed right of being informed and consulted, while the employees of SEs and SCEs have also been granted the chance to participate in the activity of the decision-making bodies of a legal person.

As mentioned above^{*65}, directives 94/45/EEC, 2001/86/EC, and 2003/72/EC have been transposed into Estonian legislation with the CSIEA, which lays down the employee involvement rules for Community-scale legal persons. The relevant regulation is very bulky, and, insofar as the directives do not leave the Member States with many options for discretion, it is also largely technical in nature. The author thus considers it unnecessary to analyse these rules further in this article, especially since the results of the surveys initiated by the European Commission in 2007 proved that the CSIEA fully complies with the requirements of the directives that served as the basis for its drafting.^{*66} The CSIEA also establishes liability in the case that the procedure for employee involvement established therein is violated.^{*67} A suitable and appropriate mechanism has thus been created in Estonia for the involvement of employees in making decisions also on the Community-scale level.

⁶¹ A shortcoming of the ECA is also the failure to lay down the employer's liability in the event of violation of the rules of informing the trustees of employees.

⁶² By the present moment, the Ministry of Social Affairs of the Republic of Estonia has developed a new Draft Employment Contracts Act, which will replace, if adopted, the existing employment contract regulation. In the new Act the employee trustees will have a guaranteed right to co-decide in the event of collective redundancies (§ 101) as well as transfer of enterprise (§ 113). The Act also foresees the employer's liability in the event of violation of the obligation of informing and consulting provided by the law in these cases (§ 128 and 129). As the employer's obligation to inform of non-typical forms of work has been left out of the Act, the Act should be complemented in that respect. Employment Contracts Act. Draft. 29.4.2008. In the web: <http://eoigus.just.ee/> (15.05.2008) (in Estonian).

⁶³ K. Jaakson, E. Kallaste (Note 18), pp. 65 and 74.

⁶⁴ The rules concerning a lawful representative body are usually applied if the parties negotiating about introducing an informing and consulting mechanism so decide, or if they fail to reach an agreement on the procedure of informing and consulting.

⁶⁵ See sub-item 2.1.

⁶⁶ Directive 94/45/EC. Directive 2001/86/EC. Directive 2003/72/EC. National Implementation Reports. Estonia. Reports elaborated by the workgroup led by Merle Muda. Studies on the Implementation of Labour Law Directives in the Enlarged European Union. Labour Asociados Consultores 2007 (reports are in possession of the author).

⁶⁷ The CSIEA among else provides liability for violation of prohibition on international informing and consulting and involvement of employees (§ 85), and for violation of obligation of annual informing and consulting and informing and consulting under exceptional circumstances (§ 87). In event of such violations the extent of liability is the same as with the violation of the rules of the general framework of informing and consulting (see Note 46).

In practice, the scope of application of the CSIEA is not very great, mainly because there are no Community-scale undertakings or groups of undertakings or SCEs with headquarters in Estonia or bearing responsibility for the Community-scale functional involvement of employees. Two SEs have indeed been established in Estonia^{*68}, but this does not include extensive application of the act. Given the state of the Estonian economy, significant changes in this respect are probably not anticipated. If Community-scale legal persons are still established, it will be difficult to forecast the level of effectiveness with which they will activate the employee involvement mechanism. As mentioned above^{*69}, local employers and employees do not have the habit of communicating with each other. Experience of the two SEs established in Estonia shows that mutual informing and consulting was considered insignificant by the competent bodies of the participating legal persons and the trustees of the employees.^{*70} Thus, the CSIEA regulation has practical meaning only in situations wherein Estonian representatives need to be elected to bodies of employee trustees from the Estonia-situated enterprises of Community-scale legal persons.^{*71}

6. Conclusions

Before accession to the EU, the concept of employee involvement was an unfamiliar phenomenon in the Estonian legal order. The entirety of the respective regulation thus rests on EU directives that are correctly transposed into national law, creating a sufficient and appropriate legal basis for employee involvement in enterprise-related decisions. In Estonia's practice, the informing and consulting of employees is, however, not common. On the one hand, this may be because the provisions related to employee involvement have been in force for only a relatively short time. A greater problem can be seen in the fact that employee trustees have not been elected at most employers or they are incompetent in co-deciding on matters concerning employment relationships and the labour market and the employer's economic activity. As the informing and consulting of employees is a new area in Estonian employment relationships and requires additional knowledge and skills on the part of the employee trustees as well as employers, it will probably take years for a constructive dialogue to develop between employees and employers.

⁶⁸ In 2007 SE Sampo Life Insurance Baltic and Seesam Life Insurance SE were entered into the commercial register in Estonia.

⁶⁹ See sub-items 3 and 4.

⁷⁰ In both cases the first meeting of the special negotiation body decided not to commence the negotiations concerning the determination of procedure for employee involvement.

⁷¹ Also see M. Muda. Estonia. – European Works Council. Kluwer Law International 2008, paragraphs 139–142.



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Processes of Modernisation of Private Law Compared, and the CFR's Influence

1. Introduction

The purpose of this article is to explain what constitutes the approach of the Czech legislator in recodifying Czech private law, and to justify my position that this is the optimal way forward. I will reach this aim through having completed a relatively extensive and broad-ranging analysis.

Having established a starting point, in the second part of the paper I point out the various possibilities of the method and address, in particular, its place in view of the background of private law in the 'new' member states of the EU, which have a recent history similar to that of the Czech Republic behind them — i.e., the influence of the Soviet model. In this part of the paper, I will attempt to show how differences, and frequently also rational influences, played their part in the further development of the private law system.

Following this, in the third section, I evaluate the significance of the Draft Common Frame of Reference (DCFR) and other national or supranational codification or similar projects. Furthermore, I continue the discussion concentrating on the Czech Republic and provide an analysis of the decisive factors related primarily to the content and method of legislation in the country's new civil code. Finally, I offer justification for the adoption of the DCFR as a model in many areas of private law for the re-codification thereof.

2. Civil law modernisation — comparison of approaches

Not only on the European level but also in the national rules of law, an enormous quantity of activity has been carried out in recent years. It is unsurprising perhaps that the most important changes in Europe over the last 10 years have been made, above all, in some new EU member countries — namely, Poland¹, Hungary²,

¹ See J. Poczybut. Zur Reform des polnischen Zivilrechts. — Zeitschrift für Europäisches Privatrecht (ZEuP) 1995, pp. 75–90.

² See L. Vékás. Über die Neugestaltung des ungarischen Zivilrechts. — J. Basedow et al. (eds.). Festschrift Drobnig. Tübingen 1998, pp. 713–723; L. Vékás. Privatrechtsreform in einem Transformationsland. — J. Basedow et al. (eds.). Aufbruch nach Europa. Tübingen 2001, pp. 1049–1064.

Slovenia³, Estonia⁴, Latvia⁵, Lithuania⁶, Slovakia⁷, and the Czech Republic.⁸ However, the individual countries chose different approaches. The only common feature in this process is represented by the effort for modernisation. Its extent and the method of its realisation, in particular, in the individual countries differ significantly. On the basis of knowledge of the individual approaches applied, we can carry out a specific classification procedure that should prove interesting for the audience. We will classify these approaches or efforts according to several criteria:

- 1) the state of the current national private law system,
- 2) the timing, and
- 3) the model for the changes and the method of their realisation.

2.1. The state of the national system of private law

2.1.1. Assessment criteria

The first aspect we assess and analyse here is a phenomenon that can be assessed or, as the case may be, evaluated from a number of standpoints. Our evaluation criteria consist in the extent of adequacy of the private law in the countries being compared with respect to the satisfaction of market — or, as the case may be, market economy — needs. In other words, we assess the private law's capability to function under new political but first of all economic circumstances in the climate following the fundamental changes of the late 1980s and/or at the beginning of the 1990s. The criterion applied here is to a substantial extent similar to another criterion — one involving the difference of the relevant private law, particularly in its codified form, from what follows the traditional understanding in this area (i.e., its difference from the concept under Roman law).⁹ Thus we will first evaluate the state of the legislation itself, subsequently turning to the area of private law theory and of the judicature.

2.1.2. Legislation

From the above point of view, we can develop the following classification:

- a) **The private law as a part of another rule of law.** This category includes the Baltic countries (Estonia, Lithuania and Latvia)¹⁰, which, after their separation from the Soviet Union at the beginning of the 1990s, found themselves to have been placed in a situation of 'total' inheritance of a foreign rule of law — that is, even in the area of civil or, as the case may be, private law, to have been left with the Soviet regulation. This 'inheritance' alone, regardless of the non-functionality or perhaps even inadequacy of the Soviet civil law legislation (in the strict sense, the legislation of the Russian Federation)¹¹, was the reason for making a swift change of the system of law. However, each of these systems followed a significantly different path. While Estonia¹² tried to adopt certain principles of the Western European legislation as its own (the Principles of European Contract Law, or PECL, in particular) and adjusted the codification, in the sense of the system, to that of pre-war times (in the law of obligations, the property law codex, etc.), Latvia¹³ took over earlier legislation — i.e., the civil code of 1937. Lithuania¹⁴ (civil code of 2000) chose a relatively distinctive way in its combination of some Western European elements with its own legal categories.

³ See V. Trstenjak. Das neue slowenische Obligationenrecht. – WGO 2002, pp. 90–110.

⁴ See L. Mikk. Zur Reform des Zivilrechts in Estland. – Jahrbuch für Ostrecht 2001, pp. 31–52.

⁵ K. Balodis. On Latvian Civil Law. – Latvian Law Review 2001, p. 58 ff.

⁶ See J. Mikelenas. Unification and Harmonisation of Law and the Turn of Millennium. – Uniform Law Review 2000, pp. 2243–2261.

⁷ See V. Lazar. K niektorým koncepčným otázkam rekodifikácie súkromného práva (On Some Conceptual Aspects of the Civil Law Recodification). – Právní praxe 2001, p. 87 ff. (in Slovak).

⁸ See, *inter alia*, K. Eliáš. Charakteristika návrhu nového občanského zákoníku (Characteristics of the Czech Draft of the Civil Code). – J. Švestka, J. Dvořák, L. Tichý (eds.). Sborník statí z diskusních fór o rekodifikaci občanského práva (Essays on the Recodification of the Civil Law). Prague 2006, p. 28 ff.; K. Eliáš, M. Zuklínová. Principy a východiska nového kodexu soukromého práva (Principles and Basis of the New Code of the Civil Law). Prague 2001.

⁹ See L. Vékás. Models in Central-Eastern European Code. – S. Grundmann, M. Schauer (eds.). The Architecture of European Code and Contract Law. Kluwer 2006, pp. 117–128.

¹⁰ See Notes 4–6.

¹¹ Principles of the civil law legislation from 1922.

¹² See Note 4 and Law of Obligations Act (võlaõigusseadus) of 26.09.2001. – RT I 2001, 81, 487 (in Estonian).

¹³ See Note 5.

¹⁴ See Note 6.

- b) **Relatively capable legislation.** At least three 'Eastern Bloc' countries have retained a relative autonomy, though each of them has done so for a different reason, as well as the quality of capability of their civil law systems. In contrast to the Czech Republic^{*15}, Poland^{*16} used in its codification work, as preparation for its civil code of 1964, both strictly scientific methods and the main European sources (German, French, and Austrian) and was affected relatively little by the Soviet example.^{*17}

Through its still valid civil code of 1959, Hungary^{*18} substantially assumed the Hungarian equity from the times of the Austro-Hungarian Empire. The Hungarian civil code was, however, significantly updated — to a level completely unprecedented at the time. Undoubtedly, it was affected by the Swiss model as well. The Hungarian civil code is brief, systematically modern, and in its abstractness capable of substantial flexibility. Slovenia^{*19} followed the Yugoslavian way, which, by contrast, was a very modern one.^{*20} As all the other Yugoslavian countries, it did not know a civil code in the current understanding of the concept; however, similarly to the Baltic countries, Yugoslavia^{*21} codified the law of obligation, family law, and substantive law, as well as the law of persons, each in a special legal regulation. Despite its lack of modern legal discourse in this area, Yugoslavia displayed a very modern understanding of the law of obligations, in particular — both in a purely technical sense, assuming the international business contract as a starting point, and with respect to the protection of the weaker party.^{*22}

In all of these countries, the existing private law legislation was very capable of functioning under the changed economic circumstances.

- c) **A peculiarly created system.** As the reader will be aware, in addition to the GDR's civil code of 1975^{*23}, it was the Czechoslovak civil code of 1964^{*24} that, from the legal concept point of view, was the most distinct attempt to deviate from the concept of civil law found in Roman law. Similarly, it is relatively well known that, from the system point of view, in particular, its concepts manifested themselves in a number of ways. It distinguished rather faithfully — i.e., in accordance with the economic situation — among the various economic law relations and adjusted the handling of civil law issues in response to the economic-political situation in the most faithful way of any Eastern European country.^{*25} The obligations were replaced with services, in other than an economic sense; the legal personality was changed and adjusted; and the obligation-related issues were adjusted to the quota economy. From this standpoint, a certain part of the civil code showed an absolute focus on protection of the weaker party. The superficies *solo cedit* principle was abandoned as a key traditional institution of property law.
- d) **Other systems of law.** Other systems include the civil law of Romania and that of Bulgaria.^{*26} Neither of these systems is original, with Romania still retaining some aspects of the French Code Civil.

2.1.3. Jurisprudence and the judiciary

The condition of legislation is, to a great extent, reflected in the level of civil-law-related jurisprudence.

- a) **Jurisprudence** includes Poland, Hungary, and Slovenia.^{*27} In all of these states, civil-law jurisprudence (legal theory) enjoys a relatively autonomous position — it does not immediately fall victim to the Communist ideology and, in fact, aids in developing (as paradoxical as this may seem) private law jurisprudence. All of these states maintained more or less intensive contacts with, and thus reflected, the free jurisprudence of the West. However, there were some authors who succumbed to the ideology or certain related illusions, and one therefore can observe a substantial difference

¹⁵ See Note 1.

¹⁶ See Note 14.

¹⁷ A. Brzozowski. – K. Pietrzykowski. Kodeks cywilny. Komentarz. Vol. I. 2nd ed. Warsaw 1999, p. 7 ff.

¹⁸ See Note 15 and G. Eörsi. Das ungarische Zivilgesetzbuch in fünf Studien. Budapest 1963.

¹⁹ See the Obligations Code enacted on 1.01.2002, No.83-4287/01.

²⁰ See the Law on Obligational Relations from 1978.

²¹ See Article 547 of ZGB.

²² See ZGB der DDR.

²³ See the Civil Code, Law No. 40/1964 Coll.

²⁴ See Notes 11, 16, 17.

²⁵ See S. Stalev. Transformation der Rechts- und Wirtschaftsordnung in Bulgarien – Probleme und Perspektiven. – ZEuP 1996, pp. 444–451.

²⁶ See Notes 14, 16, 18.

²⁷ T. Sarkózy. A kereselmi törvény esetleges koncepciója (On the Conception of Private Law). Gasdaság es Jog 1999, p. 36 (in Hungarian); E. Weiss. Konsumentenschutz und Produkthaftung. – Zeitschrift fuer rechtsvergleichung (ZfRV) 1983, p. 25 ff.

from our understanding of civil law. These illusory concepts are seen in, among other actions, the Hungarian Sarkozy's^{*28} attempt to create a socialist joint-stock company and Letowska's^{*29} approach to competition or consumer protection.

The condition of the jurisprudence of other Eastern Bloc member states witnessed a steep fall, succumbing to both ideological concepts (Knapp)^{*30} and illusory notions of a new civil law (as did Z. Kratochvíl and Karel Knap).^{*31}

- b) **The judiciary.** One can hardly observe any major differences in the judiciary between the countries considered in this article. Even the supreme courts fail to express themselves as anything more than the legislator's mouth, not daring to adopt a suprapositivist and antiformalist approach to the interpretation of law. Some provisions that are directly designed for this method of interpretation find no application at all.^{*32}

2.2. Timing of the changes

In addition to purely political or political and economic aspects, the speed of changes in private law legislation is mostly a function of the degree of adequacy of these systems for addressing the changes in the economy. The foreign legislation has clearly gained political implications in the newly independent Baltic States. Therefore, fundamentally new provisions have come into existence in the Baltic States.

Partial changes are characteristic of the remaining states examined here. Ideologically and functionally inapt provisions are deleted immediately after the landmark political changes, with the necessary categories or legal institutions added in the civil law legislation later. These changes were more dramatic where these institutions had not existed before than they were in states such as Poland, Hungary, and Slovakia^{*33}, where the socialist legislation had provided for these institutions — e.g., the pledge right.

2.3. Models for changes and their implementation

This section addresses two important aspects of the development of civil law legislation. We want to find out the extent and, above all, the sources of the changes adopted in the individual states. Therefore, we look for examples or models for the new civil law systems or their reform, while also paying attention to another important angle — the methods used to create the changes to the civil law legislation.

2.3.1. Models (templates)

According to these models, the legislation examined can be divided into three groups:

- a) **Conservative.** The states with legislation that accommodated their needs proceeded with caution. These states did not carry out (and still have not carried out) any substantial changes, and, even if some partial changes have been adopted, the approach was reserved at best — save for a few exceptions, these states have not followed any models or modified the same to accommodate for their own concepts. Many times, one can hardly consider any models wherein the changes implemented solely reflect the pragmatic approach of supplementing the existing provisions. This applies mainly to Hungary^{*34} and Poland.^{*35} The approach of Latvia in taking up again the basis of its 1937 legislation can be evaluated in similar terms. Even Lithuania^{*36} falls in this category — its approach is radical in scope but very cautious in its content.

²⁸ E. Letowska. *Prawo umów konsumenckich* (Law of Consumer Contracts). Warsaw 1999 (in Polish).

²⁹ See V. Knapp. *Vlastnictví v socialistické demokracii* (Property Rights in the Socialist Democracy). Prague 1953 (in Czech).

³⁰ See Z. Kratochvíl. *Nové občanské právo* (New Civil Law). Prague 1965 (in Czech).

³¹ See Z. Kühn. *Aplikace práva* (Application of Legal Rules). Prague 2002, *passim* (in Czech).

³² See the papers of J. Poczybut, A. Maczyński and J. Lazar from the conference held in Vienna on 10–11 October 2007. Published in: R. Welser (Hrsg.). *Privatrechtsentwicklung in Zentral- und Osteuropa*. Vienna 2008 (J. Poczybut. *Geschichtlicher Hintergrund, heutiger Stand und Perspektiven des polnischen Privatrechts*, pp. 125–140; A. Maczyński. *Die Entwicklung und die Reformpläne des polnischen Privatrechts*, pp. 115–124; J. Lazar. *Über die Reform des slowakischen Privatrechts*, pp. 31–40) and J. Rajski. *On the Need for a Progressive Harmonisation of Private Law in the European Union*. — *Juridica International* 2006, p. 20 *ff*.

³³ See Note 16.

³⁴ See Note 14.

³⁵ See Note 5.

³⁶ See Note 6.

- b) **Very progressive, second change.** The approach adopted by Estonia^{*37} involved accomplishing a second phase of modernisation through adoption of the law of obligations in 2001. Slovenia followed a similar progressive path, with a new wave of change.^{*38} Estonia^{*39} has been following a modern model, similarly to Slovenia or Yugoslavia, which took the content of the provisions of the Vienna Convention on International Sale of Goods (CBG) for its own provisions on purchase agreements
- c) **Combined approaches.** The present reformation framework of the Czech Republic can be considered very conservative or pragmatic; but, in addition to that, it is characteristic, in its draft civil code, of a system manifesting a special hybrid of several concepts. Notwithstanding the novelty of this approach, what is important is that the Czech legislator has failed to incorporate the most modern approaches, which probably have been the only ones to have found a great number of relevant applications. The Czech legislator has reflected neither the Vienna Convention on the International Sale of Goods (CISG) nor the PECL or DCFR.^{*40}

2.3.2. Implementation of the changes

All of the states considered, save for the Czech Republic and Slovakia, proceeded to reform their legislation in a manner comparable to the Western European models. The approach adopted by the majority has two distinctive features — a ‘collective’ approach to drafting and a ‘scientific’ method. This means that the reform is carried out on the basis of a certain analysis of the status quo and of a certain method for transformation, with each change having its thorough theoretical rationale. The collective approach means that a team of experts participates in the changes in a relatively similar manner (with the same rights and duties). The teams usually comprise several groups, each addressing specific parts of the civil law; the results then are discussed in a committee that, similarly to the workgroups, adopts specific decisions by consensus or by voting.

The Czech Republic, where the preparatory work started in 2001 and since 2005 the Draft of Civil Code as being amended has been published^{*41}, has chosen a very different and unique method in respect of both elements mentioned above. This is seen in various ways:

- Even with a certain basic analysis of the legitimacy of the changes and their implementation presented, the proposed provisions (i.e., the materials drafted) contain virtually no rationale.^{*42} The basic analysis is very brief and sketchy and basically addresses only the need for new legislation. The reasons for the fundamental change, although more or less ideological, will suffice at a basic level. The principles of the private law provisions published on paper do not constitute an analytic work that would display the fundamental direction for the whole future code and portions thereof — in particular, in speaking of the nature and importance of the specific legal institutions concerned. Still, the most fundamental shortcoming is the non-existence of any rationale for the language, or even the existence, of the draft. The very principles of the draft — i.e., the fundamental wording of the later draft — cannot be deemed the ideological source or the rationale for the draft, as mentioned above.^{*43}
- Drafts are compiled by individuals, which is reminiscent of certain isolated working methods (as seen in Switzerland).^{*44} Drafts are presented by an individual who has the main say in the discussion. The latest changes (with ‘mini-teams’, a co-ordination group, or the re-codification committee) hardly indicate any movements toward the standard methods of drafting legislation.^{*45}
- The fact that the text of the draft is being made available to the public for several months (on the Web pages of the Ministry of Justice)^{*46} is clearly a positive development. Everyone can look at the changes implemented. However, the procedure for implementation of these change and the reasons for these and for other changes are classified information. It is clear that the discussions or the evaluation of comments and objections are not kept on record; therefore, the work and developments associated with the draft and its changes are not transparent. This undoubtedly is in correspondence

³⁷ See Law of Obligations Act of 26.09.2001.

³⁸ Prior to the Law of Obligations Act, Estonia had adopted in 1993 the Law of Property Act (*asjaõigusseadus*). – RT I 1993, 39, 590 (in Estonian).

³⁹ Full title of CISG is United Nations Convention on Contracts for the International Sale of Goods. See Note 18.

⁴⁰ K. Eliáš, M. Zuklínová (Note 8), pp. 10–37.

⁴¹ <http://portaljustice.cz>.

⁴² Věcný záměr občanského zákoníku (Basis of the Codification of the Civil Law). – Právní praxe (Legal Practice) 2001, pp. 3–87.

⁴³ See E. Huber. System und Geschichte des schweizerischen Privatrechts. Basel 19-32-1937.

⁴⁴ Letter of the Deputy Minister of Justice of 7 December 2007.

⁴⁵ There are no (!) minutes of the sessions made.

⁴⁶ See Note 41.

with the lack of rationale in the original text of the draft. In the end, this only increases the doubts surrounding the draft itself.^{*47}

- The funding of the work is another issue.^{*48} It is remarkable that, at present, dozens of people are working on formulating the draft and its changes (even though the level of their active participation and the scope of their actual co-operation may be a matter of some doubt) and undertaking this work free of charge. In itself, this is nothing extraordinary by European standards. What is remarkable is that the project as a whole also lacks funding from the parties involved, even for out-of-pocket expenses. Nor has it been taken into account that translations will have to be made (most of the members of the current mini-teams do not even have access to relevant comparative materials or knowledge of legal language in foreign languages that is sufficient for them to make any meaningful comparisons).

2.4. Comparison

If we summarise the findings presented so far, we can reach the following conclusions:

- a) The state of private law in the individual states compared at the time of the political transformations predetermined to a significant degree the timing and degree of transformation of private law legislation. The less the state of the written civil law fit the altered socio-political conditions, the more fundamental were the changes made and the swifter the effecting thereof.
- b) Substantial changes that did not directly relate to the state of the legislative exist, however, with regard to the specimens or models of the existing or future legislative.
- c) Most of the new Member States are hesitant to undertake fundamental transformations and modernisation in the style of the supranational projects for private law. Estonia is an exception.

3. Significance of the CFR

The understanding of the significance of the Common Frame of Reference (CFR) may differ, even in the conceptions of the individual members of the Study Group. This is particularly true where this significance is evaluated in relation to the legal codes of their own legal backgrounds and the need for their modernisation. The significance of the CFR is appraised in the Czech Republic primarily from the perspective of the possibility of inspiration, influence, or assumption into the draft Czech Civil Code material.

For all of these reasons, it is necessary to ask ourselves the following basic questions:

- Why should the CFR be reflected in the field of the law of obligations?
- In the affirmative case, in what manner should it be reflected?
- To what extent do the draft and the resolution in the CFR differ?
- What are the advantages and disadvantages of reflecting the CFR, particularly with regard to further development?

3.1. Methods and illusions

For almost 100 years now, there has been an illusion of understanding the Czech Civil Code Draft as the work of an individual. Similarly, one holds an illusion of believing that there will be created an original civil code presently that fully corresponds to a specific national legislator's vision. Primarily in view of extralegal factors, law and the creation thereof is also becoming an international enterprise in the sense of its adopting models and tested methods.

One specific method applied is the method of creation of supranational projects. Here there will undoubtedly arise competition or conflict. It has been shown, however, that, although there exist a range of variation, differences in understanding and application, etc., still some fundamental, accordant understandings of the conception prevail. This is attested to by the products or the method of work of international collectives, both on the official international or inter-state basis and through 'spontaneous' platforms (academic teams).^{*49}

⁴⁷ See the letter of the Deputy Minister of Justice of 15 December 2007 addressed the author of this paper.

⁴⁸ See the famous activities as the basis of many fruitful projects in Europe: from the so-called Lando commission over ECTIL, Secola, up to Study Group on the European Civil Code.

⁴⁹ See, e.g., the law of unjustified enrichment in the Czech Draft Civil Code — 4 provisions, DCFR 15 provisions, etc. See Note 41.

3.2. Possibility of use

What O. Lando states in the foreword to the second edition of the PECL applies not only to the CFR but also to the PECL, the Principles of European Tort Law, and certain models from UNIDROIT. The possibilities for use of these projects — in particular, the CFR — are manifold. The CFR may function as model law. Even though many people contest it, its purpose and major principles 1) may lead to the adoption of several parts or institutions in national legal codes of Member States, 2) may undoubtedly serve as soft law, and 3) may have the significance of a future unified arrangement of civil law for a certain territory — maybe in Europe. The CFR may in addition, however, be a significant source for identifying law for judges and arbitrators and, finally, for study and education.

It is remarkable that many of its passages have, as regards individual provisions, the character of perfect legal norms. Therefore, the material does not involve only principles, as it would be possible for one to believe (i.e., setting forth optimising clauses); it also displays provisions having a normative character. The degree of abstraction comes remarkably close, in the aggregate of its individual parts, to a perfect normative expression of certain legal institutions. In many senses, this is a more detailed arrangement than the draft Czech Civil Code.^{*50}

3.3. Level and quality

It is possible to view a project such as the draft Czech Civil Code, but also the CFR, primarily from the system perspective. The features of both include a certain degree of homogeneity in the individual parts. The ideal, therefore, is a kind of form that is forged, as it were, from one piece. The Swiss Civil Code, the work of the sole author Eugene Huber^{*51}, is usually cited as a model. In the case of the CFR, it would be possible at first glance to conclude that the 'nature of the matter' — that is, the method of its creation (an international 'non-homogenous' community) — precludes us from following this model. In fact, however, a creative group thus heterogeneously constituted is precisely able to create a work that in its own way is internally consistent, well-arranged, and holistic. Its potential first phase is re-forged by varied opinions to offer a new quality, which affords a higher degree of harmony and unity than the work of an individual could at the present time. This is indeed the case to a greater extent with the CFR than with the draft Czech Civil Code, which to too great an extent appropriates individual provisions from various legal codes without retaining the necessary context and transformation 'at the interfaces'.

In contrast to the Czech draft, the CFR is equipped not only with a detailed rationale, which also sets forth specific cases of resolution, but also with commentary material, which maps the resolution in particular legal codes, including its advantages or disadvantages. This thus documents the quality of the outcome as a certain compromise among the best national resolutions.

The inspiration that can be provided by the CFR undoubtedly has the following merits:

- a) transparency of creation and particularly the clarity of the significance of particular provisions,
- b) the guarantee of high quality and the least possible conflict in the resolution, and
- c) guarantee of acceptance in the private law community.

3.4. The CFR and the Czech draft

3.4.1. Starting point

Private law in the Czech Republic has undergone considerable changes in the last roughly 60 years. We have the general civil code, our first phase of socialist law (the Civil Code of 1950), a second phase of socialist law (with the Civil Code of 1964 and other codices), and the transition period running from 1991 to the present.

In the briefest possible terms, I can provide a summary evaluation of the operation of these individual codification projects, thus: Practitioners (in particular, judges) were unable, possibly also as a result of the frequent changes, to make the transition from (formalistic) interpretation to teleological considerations. On the other hand, one must note the presence of a considerable degree of adaptability, not only in the field of civil law itself. This adaptability was especially evident in those areas that were beyond the scope of the civil code *per se*, particularly in legislation relating to the most rapidly developing areas, such as banking, securities, and the like. In addressing these matters, the specialist public showed great creative capability.

⁵⁰ See P. Widmer, *Helvétské úvahy nad návrhem nového českého občanského zákoníku* (Helvetic Observations on the Draft of the New Czech Civil Code). – J. Švestka, J. Dvořák, L. Tichý. *Sborník statí z diskusních fór o rekodifikaci občanského práva* (Collection of Papers on the Recodification of the Civil Law). Prague 2008, p. 123 ff. (in Czech).

⁵¹ L. Tichý. *Systémy soukromého práva a modely jeho kodifikace* (Systems of the Private Law and Models of its Codification). – J. Švestka, J. Dvořák, L. Tichý (eds.) (Note 50), pp. 42–62 (in Czech).

The result of these rapid changes, and especially the atmosphere that prevailed from the 1950s onwards, was that not even a basic theoretical foundation was created for the application of private law and the teleological interpretation thereof. The Czech Republic does not fare well if we compare the theoretical foundation present in the Czech Republic with the 'reservoir of ideas' in the traditionally revered national bodies of law. Czech theory was not even capable of bringing certain phenomena into awareness, let alone reflecting them, or accepting and developing them. There is even a substantial disparity between this state of affairs in the Czech Republic and that in other former socialist states, such as the similar legal cultures seen in Hungary and Poland, which, in comparison to our own history of development, were substantially less ruined. The latter were capable of the vital creative development of their existing positive provisions of law, such that their applicable law now offers, to a considerable degree, an adequate private law apparatus for their economic and social systems. This factor is an argument in favour of adopting the most modern solution, since the absence of a sufficiently secure 'bedrock' for the conceptual foundations of current law means that the risk of a substantial shock is relatively small.

Essentially, the present draft proceeds from these premises and is very critical of current law. The need for many amendments and the calls for further corrections testify to the unsatisfactory state of our applicable positive provisions of law and, at the end of the day, also our legal theory. However, in implementing its resolutions (see the reasoned statement accompanying the draft), it is not entirely thorough. Some areas of the draft adopt parts of the current law (e.g., language on representation; unjustified enrichment; and, with some modifications, compensation for damage). Other areas reflect the Czechoslovak model from 1937⁵², which, on account of the time of its creation and the fact that it never became applicable law, as well as the designs from which it was drawn up (in particular, the *Allgemeines Gesetzbuch der Republik Österreich*, or ABGB), cannot be considered an immediate or full-valued component of our private law tradition, being instead one of several relatively old attempts at national codification, albeit work that was of remarkable significance at the time of its creation.

3.4.2. Evaluation criterion — model

If I summarise the foregoing considerations, I reach the conclusion that it is necessary to prefer a modern approach to an approach clinging to a particular practice that, because of its superficiality and short duration, is not actually something one could invoke as a truly functioning tradition. I therefore make my evaluation of the Czech draft primarily through the prism of modern supranational legislation or drafts thereof (particularly the CFR), whereas I measure up the field of rights *in rem* — which is not part of the supranational codification efforts — primarily against the benchmark of a system of law that has a remarkable tradition and relationship with Czech law; that is the law of Austria. Several factors speak in favour of using supranational projects as a benchmark and model solution (although not as a pattern for verbatim transposition):

- a) although there is compromise involved, the supranational projects are the result and reflex of national solutions developed by absolute experts on the basis of long-term experience;
- b) in several cases, the fundamental basis used is the applicable law (CISG), or projects that, although not applicable law, are nonetheless applicable as law (as in the case of the UNIDROIT principles); and
- c) in many fields, the development is aimed at a gradual harmonisation or even unification of private law.

3.4.3. Method of reflection

Two final considerations should be applied in moving forward from the discussion here:

- a) The principles are often actually very general clauses; in most cases, however, these are functional legal norms.
- b) Reflection does not mean a slavish assumption. Even particular clauses are suitable for flexible adaptation.

⁵² See the Draft Civil Code in: F. Rouček, J. Sedláček (eds.). *Komentář k československému obecnému zákoníku občanskému* (Commentary on the Czechoslovak General Civil Code). 5 volumes. Prague 1937 which includes the draft of the "new" Czechoslovak Civil Code.



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The Buyer's Free Choice Between Termination and Avoidance of a Sales Contract

1. Introduction

National private law systems of European Union member states have different approaches with respect to freely allowing or restricting the concurrence of avoidance for mistake and termination of contract. For instance in Germany¹, upon sale of a defective thing, the priority of applying a contractual legal remedy applies, and termination is either excluded or significantly restricted, even though a case of mistake *per se* would actually exist. The Austrian and Swiss civil codes, however, allow free concurrence of such claims; in Spain and Italy, juridical practice has recognised the right of one party — the buyer — to choose the most suitable remedy.² There are no provisions in the Estonian Law of Obligations Act³ (LOA) or the General Part of the Civil Code Act⁴ (GPCCA) that would prevent the entitled party from using the most suitable remedy if both termination and avoidance are simultaneously available. Conflicting viewpoints have, however, been expressed on this matter in Estonian legal discourse.⁵

Differing positions with respect to this question have also been assumed in the uniform law instruments (UNIDROIT Principles of International Commercial Contracts⁶ (PICC), Draft Common Frame of Refer-

¹ F. Ranieri. *Europäisches Obligationenrecht*. 2. Aufl. Springer 2003 pp. 344–345.

² *Ibid.*, pp. 350, 364.

³ *Võlaõigusseadus*. – RT I 2001, 81, 487; 2007, 56, 375 (in Estonian).

⁴ *Tsiviilseadustiku üldosa seadus*. – RT I 2002, 35, 216; 2007, 24, 128 (in Estonian).

⁵ I. Kull and I. Parrest believe that “in the light of the general principles of the law, the regulation included in the special part of the LOA as *lex specialis* should have primacy over the institution of mistake.” See I. Kull, I. Parrest. *Teatamiskohustus võlaõigusseaduse kontekstis* (Notification Obligation in the Context of the Law of Obligations Act). – *Juridica* 2003/4, p. 219 (in Estonian). M. Käerdi believes that in principle, a person has the right to choose. See M. Käerdi. *Eksimuse käsitus tsiviilõiguses* (Treatment of Mistake in Civil Law). Tallinn 2002, p. 68 (in Estonian). In the comments to the Law of Obligations Act it is expressed that “an obligee may have the [...] possibility to choose between a legal remedy and between avoidance of contract [...] for mistake. See P. Varul, I. Kull, V. Kõve, M. Käerdi. *Võlaõigusseadus I. Kommenteeritud väljaanne* (Law of Obligations Act I. Commented edition). Tallinn 2006, p. 322 (in Estonian). It is said in the comments to the Law of Obligations Act regarding sales contracts that in principle, the buyer has a choice, but the general assumption should be that avoidance is against good faith in the event of absence of substantive case of fundamental breach of contract required for termination. See P. Varul, I. Kull, V. Kõve, M. Käerdi. *Võlaõigusseadus II. Kommenteeritud väljaanne* (Law of Obligations Act II. Commented edition), Parts 2–7 (§§ 208–618). Tallinn 2007, p. 38 (in Estonian).

⁶ Available at <http://www.unidroit.org/english/principles/contracts/main.htm> (1.05.2008).

ence^{*7} (DCFR), and Vienna Convention on Contracts for the International Sale of Goods^{*8} (CISG)). Pursuant to Article 3.7 of the PICC, for instance, a party is not entitled to avoid a contract on grounds of mistake if the circumstances on which that party relies afford, or could have afforded, a remedy for non-performance; i.e., the primacy of a contractual remedy applies. Pursuant to DCFR II.–7:216, however, a person is entitled to freely choose the most suitable remedy. With regard to the CISG, European Union member states have applied different interpretations regarding the relations and primacy of the right of termination of contract in relation to the right of avoidance of a contract governed by national law.^{*9} The above suggests that the prerequisites for and consequences of termination and avoidance of contracts require a comparative approach and clarification, as do situations of fact wherein the compositions of both termination and avoidance may be simultaneously fulfilled.

This article analyses the institutions of termination and avoidance of contract through the example of a sales contract, because, in practice, the choice between these two institutions causes the most problems in the context of a sales contract. Because of the limited scope of the article, it discusses only the legal remedies belonging to the buyer. The task of this research project does not include the specific types of sales contract, such as sale on approval, sale with right of repurchase, or the differences related to consumer sales — except by reference to a single characteristic example. As an example for grounds for avoidance, this article examines only mistake as one of the most commonplace grounds for avoidance of sales contract in practice, other possible grounds for avoidance are not looked at.

The article aims to determine whether in Estonian private law it would be necessary to set forth certain priorities or restrictions regarding the choice between these two legal remedies, or can justification be found for the DCFR rule that a person may choose freely between these legal remedies? The article therefore discusses the more significant problems concerning the possible priority between termination and avoidance, or the allowing of free choice between them. The study's hypothesis argues that establishing the priority of one institution over another with no exceptions is unjustified, and that in specific cases possible restrictions for preferring one over another can proceed only from general principles of civil law, primarily from the principle of good faith. With regard to the Estonian legal order, we proceed from the presumption that there cannot be an *a priori* right or wrong solution regarding the relationship between avoidance and termination. This does not, however, exclude the possibility that in other legal orders the same question could not be governed differently, depending on the peculiarity of the given order in question.^{*10}

2. Comparison of material grounds for termination and for avoidance

2.1. The possibility of simultaneous presence of grounds for termination and for avoidance

Concurrence of avoidance of sales contract and contractual claims (primarily termination, but in single cases also avoidance for mistake and the claim for amendment of contract pursuant to the *clausula rebus sic stantibus* doctrine^{*11}) emerges in the event that the circumstances of fact make up both legally relevant cases. This is primarily possible where a circumstance related to any characteristics of a sold thing that the buyer or the buyer and seller together assumed in error also becomes a condition of the sales contract and, in the event the given circumstance differs from reality, entails breach of contract by the seller and, thus, liability of the seller.^{*12} This constitutes a situation in which a flaw in the object sold, deemed to be fundamental breach, also constitutes a relevant mistake for the purposes of GPCCA § 92 and DCFR II.–7:201 — i.e., erroneous assumption of existing facts, whether caused by the other party, recognised by the other party, or commonly assumed if, the actual circumstances having been known, the transaction would not have been concluded in the first place or would have been concluded under materially different conditions, and the mistaken party does not bear the risk of mistake. An example could be employed from the official comments to the PICC^{*13} wherein A, a farmer, who

⁷ C. von Bar, E. Clive, H. Schulte-Nölke (eds.), Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference (DCFR) Interim Outline Edition III. München: Sellier 2007. Available at http://www.law-net.eu/en_index.htm (28.04.2008).

⁸ Ühinenud Rahvaste Organisatsioon konventsioon kaupade rahvusvahelise ostu-müügi lepingute kohta. – RT II 1993, 21/22, 52 (in Estonian).

⁹ F. Ranieri (Note 1), pp. 363, 375.

¹⁰ P. Huber. Die Konkurrenz von Irrtumsanfechtung und Sachmängelhaftung im neuen Schuldrecht. Festschrift für Walther Hadding. Walter de Gruyter Verlag 2004, p. 105.

¹¹ On the distinguishing between the institutions of *clausula rebus sic stantibus* and mutual mistake, see M. Käerdi (Note 5), pp. 71–73.

¹² P. Varul *et al.* Law of Obligations Act I (Note 5), p. 37.

¹³ Available at <http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=13637&x=1> (13.05.2008).

finds a rusty cup on the land sells it to B, an art dealer, for 10,000 euros. The high price is based on the assumption of both parties that the cup is made of silver, as other silver objects had previously been found on A's land. It subsequently emerges that the object in question is an ordinary iron cup worth only 1000 euros. Accordingly, B refuses to accept the cup and to pay the agreed price, on grounds that it does not comply with the terms of the contract. B also avoids the contract on grounds of mistake as to the quality of the cup.

The following differences can be found between the elements of the compositions of termination of sales contract and avoidance of sales contract for mistake: 1) the right of termination emerges if the problem lies in the performance of a concluded, valid contract (LOA § 101 (1) 4), § 116 (1), DCFR III.–3:501) whereas the right of avoidance for mistake emerges if the problem is related to the conclusion of the contract^{*14} (pursuant to GPCCA § 92 (3) and DCFR II.–7:201); 2) termination presupposes a fundamental breach of contract (pursuant to LOA § 116 (2) and § 223, and DCFR III.–3:502 (1)), with the presence of a fundamentally erroneous assumption of actual circumstances upon entry into a transaction being required as grounds for mistake (i.e., in the presence of a correct assumption, the transaction would not have been entered into at all or would have been entered into under different conditions (pursuant to GPCCA § 92 (1) and (2), as well as DCFR II.–7:201 (1) (a)); and 3) if one of the grounds for identifying a material breach of contract, prerequisite for termination, pursuant to Estonian law, constitutes failure to eliminate initial (also immaterial^{*15}) non-performance by the additional term (LOA § 114 and § 116 (2) 5), and § 223 (1)), avoidance for mistake is not related to the possibility of eliminating the non-conformity, although the other party is able to eliminate the grounds for avoidance of contract by recognising the contract as understood by the mistaken party (GPCCA § 93, the same in DCFR II.–7:203). These differences, and also similarities of compositions, are discussed next, in sections 2.2–2.3 of this paper.

2.2. Fundamental breach and fundamental mistake

Application of termination as a contractual remedy generally presupposes fundamental non-performance of a contractual obligation (see LOA § 116 (1), the Civil Code of the Federal Republic of Germany^{*16} (BGB) § 323 (1) and (5), the Civil Code of Holland^{*17} (BW)'s Article 6:265 (1), CISG Article 49, PICC Article 7.3.1 (1), and DCFR III.–3:502 (1)). As an exception we can cite English law, under which the right of termination depends not on the severity of the breach but on the type of contractual obligation breached.^{*18}

With regard to sales contracts, a breach of contract can be related to delay of performance of obligation and to unsatisfactory performance. The Estonian Law of Obligations Act, unlike the BGB, CISG, and PICC, enables turning a non-fundamental unsatisfactory performance into a fundamental breach of contract through an additional term for elimination of flaws given to the obligor (LOA § 116 (2) 5), and with regard to sales contracts this mostly constitutes the claim for repair of a thing, LOA § 223^{*19}). However, pursuant to DCFR III.–3:503, the institution of fixing an additional period of time is primarily related to delay in performance. That Estonian law allows deeming an immaterial unsatisfactory performance to be a fundamental breach of

¹⁴ See also M. Käerdi (Note 5), p. 73: "[a] mistake always presupposes a non-conformity between the actual situation during entering into a transaction and the situation constituting the content of the declaration of intent aimed at entering into the transaction."

¹⁵ V. Kõve. Lepingu ühepoolse lõpetamise võimalused Eesti õiguses (võrdlev käsitus). Magistritöö (Possibilities of Unilateral Termination of Contract in Estonian Law (comparative approach). Master's Thesis). Tartu 2003, p. 125 (in Estonian); P. Varul *et al.* Law of Obligations Act I (Note 5), p. 402.

¹⁶ BGBI 1896, 195.

¹⁷ Entered into force on 1.01.1992.

¹⁸ H. Sivesand. The Buyer's Remedies for Non-conforming Goods. Sellier. – European Law Publishers 2005, pp. 73, 79.

¹⁹ LOA § 116: "(2) A breach of contract is fundamental if:

1) non-performance of an obligation substantially deprives the injured party of what the party was entitled to expect under the contract, except in cases where the other party did not foresee such consequences of the non-performance and a reasonable person of the same kind as the other party could not have foreseen [...] consequences under the same circumstances;

2) pursuant to the contract, strict compliance with the obligation which has not been performed is the precondition for the other party's continued interest in the performance of the contract;

3) non-performance of an obligation was intentional or due to gross negligence;

4) non-performance of an obligation gives the injured party reasonable reason to believe that the party cannot rely on the other party's future performance;

5) the other party fails to perform any obligation thereof during an additional term for performance specified in § 114 of this Act or gives notice that the party will not perform the obligation during such term."

"§ 223: (1) The seller is deemed to be in fundamental breach of a sales contract also if, inter alia, the repair or substitution of a thing is not possible or fails, or if the seller refuses to repair or substitute a thing without good reason or fails to repair or substitute a thing within a reasonable period of time after the seller is notified of the lack of conformity. (2) In the event of customer sale, any unreasonable inconvenience caused to the buyer by the repair or substitution of a thing is also deemed to be a fundamental breach of contract by the seller. (3) In the cases specified in subsections (1) and (2) of this section, the purchaser is not required to determine an additional term specified in § 114 of this Act and has the right, inter alia, to withdraw from the contract."

contract has been pointed out by Justice of the Supreme Court Villu Kõve.^{*20} It has also been found in the comments to the Law of Obligations Act that such a regulation may not be just or justified, and reference has been made to the necessity of amending such a regulation.^{*21} At the same time, the misuse of the right of relevant termination is nevertheless restricted by the principle of good faith^{*22} which, pursuant to LOA § 6, also has the primacy over the law and certainly mitigates the severity of this problem.

Keeping in mind the principle of good faith, Estonian legal discourse has also expressed the viewpoint that the possibility of avoidance for mistake cannot be considered justifiable in a situation where the buyer has no right to terminate the contract on account of non-materiality of the breach but, because of mistake, avoidance could be possible.^{*23} A situation in which a circumstance does not constitute a fundamental breach of contract in a contractual relationship but at the same time can objectively be determined to be a relevant mistake for a reasonable person^{*24} should in reality occur relatively seldom. It is more likely that if certain breach by a seller must be regarded as immaterial, the same situation generally does not include elements of a relevant mistake for a reasonable person. Namely, the standard of a reasonable person is to be implemented normatively, comprising the value judgements of the society^{*25}, and, that being the case, lower standards than those applied upon evaluation of the fundamentality of the breach by a certain party to the contract in a similar situation should not generally be presumed to be established. Considering the above, we do not find it justifiable or necessary to restrict the possibility of avoidance with dependence on the occurrence of a fundamental breach of contract in the same factual circumstances.

2.3. Knowledge of circumstances of breach or of mistake, and allocation of risk between parties

Modern transaction theory^{*26} often supports the possibility of using various legal institutions and legal remedies on the principle of risk allocation.^{*27} With regard to avoidance, it is worth bearing in mind that if, as a rule, persons themselves bear the risk that their intention has been formed by means of correct assumptions and, in view of all circumstances, the person's right of avoidance will nevertheless be considered to be an exception if the mistake has been caused by the other party or is mutual (see, for example, DCFR II.–7:201 (1) (b), PICC Article 3.5, BW Article 6:228, and GPCCA § 92 (3)). In these cases, the trust in the contract remaining valid does not deserve protection^{*28}. At the same time, avoidance of contract is excluded if the mistake concerns circumstances the risk of which is borne by the mistaken party (pursuant to GPCCA § 92 (5) and also DCFR II.–7:201 (2) (b)), meaning those belonging to said party's sphere of influence.^{*29} Similarly, termination as a legal remedy is excluded in the event that the non-performance underlying the termination has been caused by the party wishing to terminate the contract or it belongs to its own sphere of influence.^{*30} With regard to sales contracts, this principle is specified in LOA § 218 (4), which provides that the lack of conformity of a thing does not provide grounds for application of contractual remedies to the seller if the buyer was or ought to have been aware of the lack of conformity of the thing upon entry into the contract. A similar principle is established in DCFR III.–3:502 (2) (a). The buyer's awareness or obligation of awareness of the non-conformance of a thing at the time of entry into a sales contract thus excludes the buyer's right of termination of the sales con-

²⁰ V. Kõve (Note 15), p. 125.

²¹ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 402.

²² I. Kull. Hea usu põhimõte kaasaegses lepinguõiguses (Principle of Good Faith in Modern Contract Law). Tartu University Press 2002, pp. 168–174 (in Estonian).

²³ P. Varul *et al.* Law of Obligations Act II (Note 5), p. 38.

²⁴ Fundamental breach of contract, as a basis for termination, is determined in law as a partially subjective criterion depending on what the *injured party* was entitled to expect under the contract, or what was the precondition of his continued interest (LOA § 16 (2)); however, in identifying a relevant mistake, only the objective criterion — a reasonable person — is followed (GPCCA § 92 (2)).

²⁵ M. A. Simovart. The Standard of Reasonableness in Estonian Law. – I. Kull (ed.). Development of Estonian Contract and Company Law in the Context of the Harmonized EU Law I. Tartu 2007, p. 69.

²⁶ This can be opposed by the classical transaction theory, which mainly proceeds from the intention theory and which consider a mistake to constitute the divergence between a person's actual intention and the objective declaration of intent. See K. Saare, K. Sein, M. A. Simovart. Differentiation of Mistake and Fraud as Grounds for Rescission of Transaction. – *Juridica International* 2007/1, p. 143. This article only comparatively discusses the institution of mistake based on the viewpoints of contemporary transaction studies, and termination as a legal remedy.

²⁷ K. Sein. Ettenähtavus ja rikutud kohustuse eesmärk kui lepingulise kahjuhüvitise piiramise alused. Doktoritöö (Foreseeability and the Purpose of the Obligation Theory as Grounds for Limitation of Damages in Contractual Relationships. Dissertation). Tartu 2007, p. 97 (in Estonian).

²⁸ K. Saare *et al.* (Note 26), p. 143.

²⁹ On the principles for determination of risk allocation see K. Sein (Note 27), pp. 97–103.

³⁰ LOA § 101 (3): "An obligee shall not rely on non-performance by an obligor nor resort to legal remedies arising therefrom insofar as such non-performance was caused by an act of the obligee or by circumstances dependent on the obligee or by an event the risk of which is borne by the obligee."

tract; neither can the buyer in such cases avoid contract for a fundamental mistake, as in that case the buyer will bear the risk of the mistake (GPCCA § 92 (5), DCFR II.–7:201 (2) (b)).

The principle that restricts or excludes the possibility of avoiding a contract for mistake in a situation in which the mistake is caused by the mistaken party — i.e., where the mistaken party bears the risk of mistake — is recognised by some other European countries besides Estonia.^{*31} The above can be considered the view of contemporary transaction studies addressing the questions of mistake, but this view is not, however, widespread.^{*32} The mistake-related provisions of the DCFR have been drawn up for the purpose of achieving a justified balance between the voluntary nature of a contract and the reasonable expectations of the other party.^{*33} It is considered unfair to give a person the right to avoid the contract if that person has mainly caused the mistake, except if the other party can be at least equally 'blamed' for causing the mistake.^{*34} Among the more important key concepts related to delimiting the possible common compositions of termination of sales contract and avoidance of sales contract are the allocation of risks between the parties and satisfactory performance of the duty to inform by the seller. If a buyer's erroneous assumption of the actual qualities of a thing has been the result of a circumstance the risk of which is borne by the buyer, avoidance of the sales contract for mistake is excluded by the buyer directly. This situation resembles (but is not necessarily identical to) the buyer's obligation of awareness of the flaws of the object of the sales contract, excluding avoidance of the contract by the buyer as a legal remedy.

It must be noted that overlap of termination and avoidance of sales contract does also not occur if the circumstance underlying the mistake does not become a condition of the contract — e.g., if the buyer during pre-contractual negotiations refers to qualities of the thing that are not present in reality and if in the sales contract itself all previous agreements and promises are excluded (LOA § 31).^{*35} In this case, the buyer would merely retain the right to avoid the contract, the grounds for avoidance being the circumstances that were reported by the other party during the pre-contractual negotiations and that influenced the mistaken or deceived party to the contract in the direction of entering into a contractual relationship. Termination of contract is not possible in such a case, as there is no breach of the contract itself.

The analysis above has shown that termination and avoidance can be possible in one and the same factual situation. It is nevertheless unclear whether a buyer who, presumably, could be entitled to both avoidance and termination of a sales contract is legally allowed to resort to one of these two choices at his own discretion, or should the law set forth a mandatory provision as to which of the two to prefer? In order to clarify this question, we next examine whether differences are present in the implementation of the two institutions, and what they are, and the extent to which such differences influence the interests of either party.

3. Execution of termination and avoidance

3.1. Form and content of notices of termination and avoidance

Both termination and avoidance occur by an entitled person's submission of notice to the other party (LOA § 188 (1) and GPCCA § 98 (1)); i.e., in both cases we are dealing with a unilateral formative right and not claims.^{*36} As this is a formative right, neither of the rights is subject to a limitation period.^{*37} Termination and avoidance are set forth as a self-help right remedies also in DCFR II.–7:209 and III.–3:507, with the same being done in the national laws of many European countries, among them the United Kingdom^{*38}, Ireland, the Czech Republic, Finland, Sweden, Portugal, Holland, and Spain.^{*39} Under Scottish law, it is sufficient

³¹ DCFR II.–7:201, Notes VIII–41, 42, Comments, A.

³² Germany and Switzerland, for instance, do not proceed from the principles of modern transaction theory upon discussing mistake. See DCFR II.–7:201, Notes VIII–43.

³³ DCFR II.–7:201, Comments, A.

³⁴ DCFR II.–7:201, Comments, J. Identification of the so-called self-induced mistake is dependent upon both the content of the transaction and the circumstances of entering thereinto.

³⁵ P. Varul *et al.* Law of Obligations Act II (Note 5), p. 38.

³⁶ In the case of some types of transaction, avoidance of contracts by unilateral declaration of intent is either excluded or restricted under Estonian law. In those cases, special regulation is applied in the form of subjecting to court or other dispute resolving authority (e.g., contracts of employment pursuant to § 125 (1) of the Contracts of Employment Act (*töölepingu seadus*). – RT 1992, 15/16, 241; RT I 2007, 44, 316, (in Estonian); marital property contracts pursuant to § 11 of the Family Law Act (*perekonnaseadus*). – RT I 1994, 75, 1326; 2006, 14, 111 (in Estonian).

³⁷ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 411.

³⁸ See J. O'Sullivan. Rescission as a self-help remedy: a critical analysis. – Cambridge Law Journal 2000 (59), pp. 509–543.

³⁹ DCFR II.–7:209, Notes, 2; III.–3:507 Notes I–2.

for termination if a person behaves in such a way as to implicitly declare the contract terminated.^{*40} On the other hand, for instance, French and Austrian law require, as a general rule, a court decision in order for a transaction to be avoided^{*41}, and in several countries (e.g., Belgium, Luxembourg, and Italy) a contract may be terminated also by a court decision.^{*42}

Estonian law does not set forth specific requirements related to the content or form of a notice of termination and avoidance.^{*43} Thus, a buyer may, for instance, terminate or avoid a notarised sales contract by submitting an unattested notice to the seller. Furthermore, the LOA's § 13 (2) provides that if a contract is entered into in a specific format pursuant to an agreement between the parties, amendment or termination of the contract need not be in such a format — similarly, it may be presumed that the parties are not required to adhere to the form they have agreed upon in the case of giving notice of termination (as essentially unilateral termination). Notice of termination may, pursuant to the commentaries to the LOA, also be conclusive^{*44} or given in the form of an indirect declaration of intent as defined in GPCCA § 68 (3); however, the authors still find that “the power of a self-help remedy cannot be vested in an ambiguous [...] declaration of intent, as the exercise of such a right must be clear”.^{*45}

At the same time, in the case of the CISG, it is not unambiguously clear whether an indirect declaration is sufficient for termination. On the one hand, it has been found that, on the basis of the general principles of the CISG, mutual notification is crucial^{*46}, but, on the other hand, because of the principle of freedom of form, an indirect declaration of intent should be acceptable for termination, provided that it has been ‘communicated’ to the other party and that it is clearly understandable — for instance, the mere return of the goods supplied cannot be interpreted as valid termination, because the conclusions that can be drawn from such an act may differ.^{*47} Court practice exists pertaining to termination notice given under CISG Article 49; however, the conclusions that have been drawn are somewhat inconsistent.^{*48} Nevertheless, in order to terminate a contract, the related declaration of intent need not directly refer to termination.^{*49}

Neither does Estonian law establish very clear requirements as to the exact content of a termination or avoidance notice — what is important is that the intent of the person be comprehensible. It is not required that a person refer to the legal basis (relevant provision of law) for his claim, nor is it necessary to express the actual reason underlying the termination.

In connection with the above, however, the following problem arises: if a person expresses the intent to **be free from the contract**, without specifying the legal content, then how should one interpret such a declaration — as termination or as avoidance of a contract? The authors of the commentaries to the LOA hold the position that there is no problem concerning the understandability of the content of a declaration of intent if termination is referred to as ‘termination of the contract’, ‘suspension of the contract’, or ‘discontinuance of the contract’, because all of these expressions refer to the cancellation of an existing contract. They do, however, accept tacitly that there may be a problem in delimiting a declaration of intent from avoidance^{*50}. This may prove to be especially complicated where the parties use English for communication purposes, because certain terminological inconsistencies may be observed in English-language materials that deal with termination and avoidance.^{*51} Some problematic terms in this context are ‘termination’, ‘nullification’, ‘repudiation’,

⁴⁰ DCFR III.–3:507, Notes I–2.

⁴¹ F. Ranieri (Note 1), p. 336. The same regulation was effective in Estonia before the entry into force of the new GPCCA in 2002.

⁴² DCFR III.–3:502, Notes I–1, III.–3:507, Notes I–3.

⁴³ CCSCd, 19 April 2006, 3-2-1-29-06, p. 20; CCSCd, 12 June 2006, 3-2-1-50-06, p. 23; CCSCd 3-2-1-59-06, p. 16; CCSCd, 13 February 2008, 3-2-1-140-07, p. 35.

⁴⁴ CCSCd 3-2-1-50-06.

⁴⁵ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 623.

⁴⁶ L. A. DiMatteo, L. Dhooge, S. Greene, V. Maurer, M. Pagnattaro. The Interpretive Turn in International Sales Law: An Analysis of Fifteen Years of CISG Jurisprudence. – Northwestern Journal of International Law and Business 2004 (34), pp. 299–440, p. 434, footnote 646. Available at <http://www.cisg.law.pace.edu/cisg/biblio/dimatteo3.html#646>.

⁴⁷ U. Magnus. Remedy of Avoidance of Contract under CISG — General Remarks and Special Cases. – Journal of Law and Commerce 2005–2006 (25), p. 427.

⁴⁸ L. A. DiMatteo *et al.* (Note 46), p. 405.

⁴⁹ For instance, a court decision dated from 3.03.1989, treated as a declaration of intent the telegram sent by a purchaser where he unambiguously declared that in the future he would buy similar goods (shoes) from another manufacturer and terminated co-operation with the seller. The seller who was in breach of the contract could not doubt, because of the circumstances surrounding the case, that the purchaser refused to accept the goods supplied by the seller and therefore the purpose of dispatching the goods remained unfulfilled. It is sufficient that the notice given by the purchaser is clear on the point that due to the seller's breach of the contract the purchaser will not pay the seller because the supply of goods has become useless for the purchaser. Germany, 17 September 1991, Appellate Court Frankfurt (Shoes case). Available at <http://cisgw3.law.pace.edu/cases/910917g1.html>.

⁵⁰ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 623.

⁵¹ H. Sivesand (Note 18), p. 9.

‘cancellation’, ‘rescission’, and ‘avoidance’. It is notable for instance that the CISG and related literature use the term ‘avoid’ in the meaning of termination of a contract.^{*52}

The authors of this article believe that if interpretation really would be of no avail in ascertaining which of the two alternatives the person had in mind when giving notice — especially in a situation where the said person was actually unaware of the two potentially differing implications of the notice, one should proceed from the principle of good faith and take the position that the person made the declaration that is more favourable to him.

3.2. Temporal limits on termination and avoidance

Insofar as the institutions of both termination and avoidance significantly affect the future relationship between the parties and their trust in the continuing validity of the contract, the exercise of both is temporally limited. Termination as a legal remedy is regulated by LOA § 116 (1) and provisions complementing it — namely LOA § 223 and § 226 in case of a sales contract — and it occurs by submitting a notice of termination to the other party to the contract. Similar provision can be found in DCFR III.–3:503. A notice of termination should be preceded by notification of the seller as to any lack of conformity of a thing within a reasonable period after the buyer became or should have become aware of the lack of conformity (LOA § 220 (1)). The buyer reserves the right to termination without prior notification of lack of conformity only in some exceptional cases (LOA § 221 (1) 1)–2)).

The buyer’s obligation to report any lack of conformity also holds under German law and is one of the reasons that in Germany the priority of a contractual legal remedy is honoured: it is believed that if the buyer were entitled to avoid a contract of sale irrespective of his failure to notify the seller in a timely manner of any lack of conformity, the entire system of regulation of termination and the obligation of notification as to lack of conformity would be rendered senseless.^{*53} Such argumentation is only partially transferable into Estonian law. The authors believe that in the case of a mistake caused by the seller or in that of a recognised mistake (GPCCA § 92 (3) 1) and 2)), free competition between termination and avoidance should be allowed because in that case, similarly to those of intent on the part of the seller, gross negligence, or breach of the notification obligation, the buyer is free to terminate the contract even if he fails to comply with the obligation to notify the other party of lack of conformity (LOA § 221 (1)^{*54}). In the case of a mutual mistake (GPCCA § 92 (3), 3)), if the circumstances cannot be attributed to the seller, it is theoretically possible to apply the principle of good faith and accept the priority of a contractual legal remedy: However, for practical reasons, such a distinction between different types of mistake is inexpedient or altogether impossible — upon becoming aware of a mistake, the buyer need not necessarily know whether it was his own or a mutual mistake.

In connection with the time limit on termination, one also faces the question of whether the buyer who fails to comply with the deadline agreed upon between the parties for the inspection of a thing and for notification of any lack of conformity (e.g., two weeks after delivery of the goods) will, in addition to suffering the loss of the right to terminate the contract, also lose the option of avoiding the contract on the basis of the existence of a mistake, although under GPCCA § 99 (1) 2) said party still has time to exercise that right (as six months have not passed since he became aware of the mistake). The authors believe that the matter depends on the content of the agreement between the parties, which needs to be clarified by way of interpretation. If the agreement concerned just the deadline for termination, there is no basis for extending it to avoidance; if this is the case, the buyer will reserve the right to avoid the contract on the basis of a mistake also after the deadline specified in the contract has passed.

At the same time, the authors also believe that in principle it is possible to agree on the deadline for exercise of the right of avoidance on the basis of a mistake, and thus the parties may agree on a deadline other than set out in GPCCA § 99 (1) 2).

Until now, Estonian legal theory has not studied the issue of applicability of party autonomy towards the deadline for avoidance based on a mistake, nor is there any related Supreme Court practice. The authors of this article believe that extending party autonomy to this rule should not be considered to be contrary to the spirit of the law or violate the fundamental rights of the parties concerned, i.e., the parties should be entitled to determine the time period during which avoidance based on mistake is acceptable. This would not be the

^{*52} CISG Advisory Council Opinion No. 5, footnote 9. Available at <http://www.cisg.law.pace.edu/cisg/CISG-AC-op5.html#9>.

^{*53} Münchener Kommentar zum Bürgerlichen Gesetzbuch. Band I: Allgemeiner Teil. 5. Aufl. Commenter: Kramer. C. H. Beck 2006, § 119, margin number 33.

^{*54} LOA § 221: “(1) A purchaser may rely on the lack of conformity regardless of the purchaser’s failure to examine a thing or give notification of the lack of conformity of the thing on time if:

1) the lack of conformity of the thing has been caused by the intent or gross negligence of the seller;

2) the seller is aware or ought to be aware of the lack of conformity of the thing or the circumstances related thereto and does not disclose such information to the purchaser.”

case with other grounds for avoidance, such as fraud or taking advantage of aggravating circumstances. The position that the regulation of the deadline for the right of avoidance on the ground of mistake should be treated as dispositive is in accord with DCFR II.–7:215 (2), according to which remedies for mistake may be excluded or restricted unless that exclusion or restriction is contrary to good faith and fair dealing. Therefore, the parties to a transaction are free to agree on a deadline for avoidance on the basis of a mistake that differs from that provided for by the law.

Neither does Estonian law preclude freedom of such agreement, and thus the authors believe that, as a general rule, the parties may agree on a deadline for avoidance that is either shorter or longer than that provided for in the law.

Another factor considered in German law to justify the priority of contractual legal remedies is the requirement that, unlike avoidance, termination must as a rule be preceded by notification of the other party of an additional deadline for proper performance of the contract.^{*55} The requirement of granting an additional deadline is also present in Estonian law (LOA § 116 (4), § 114, and § 222, as well as § 223 (1)). If an additional deadline is not granted, termination is allowed in all of the cases cited in LOA § 116 (2) 1)–4), including the case where “pursuant to the contract, strict compliance with the obligation that has not been performed is the precondition for the other party’s continued interest in the performance of the contract” (LOA § 116 (4), 2nd sentence and § 116 (2) 2)) or where the other party gives notice that said party will not perform the obligation (LOA § 116 (4), 2nd sentence). In the event of other types of fundamental breach of contract^{*56}, termination of the contract without granting of an additional deadline for performance is prohibited if the damage suffered by the non-performing party in the event of termination would be disproportionate in relation to the expenses incurred in the performance or preparation for the performance of the obligation (LOA § 116 (4)). When an additional deadline for performance is granted, it must be reasonable (LOA § 114 (1)). The reasonableness of such a deadline is decided upon on the basis of the general regulation provided in LOA § 7^{*57}, taking into account all of the circumstances specified therein.^{*58} Language regulating an additional period of time of reasonable length is also contained in, for example, articles 47 and 53 of the CISG. The obligation to grant an additional deadline — if it exists — distinguishes the procedure of termination from that of avoidance: The GPCCA does not provide for such an obligation in the case of avoidance on the basis of a mistake.

Nevertheless, the GPCCA’s § 93 provides the other party with the option of understanding performance of the transaction as desired by the mistaken party. If this is the case, the option of avoidance is lost (GPCCA § 93 (1)), or, if the right of avoidance has already been exercised, the notice of avoidance shall be deemed invalid (GPCCA § 93 (2)). For instance, a buyer who has entered into a contract on the sale of an immovable discovers, after signing the contract, that the immovable is polluted. The seller failed to disclose this fact to the buyer when the two parties signed the contract and, thus, the buyer submits a notice of avoidance relying on the mistake. If after receiving the notice of avoidance the seller promptly gives notice of his willingness to remove the pollution at his own cost — i.e., to perform the contract on sale as understood by the buyer — the buyer’s notice of avoidance should be deemed invalid and the contract shall be deemed valid on the condition that the seller transfers the immovable free of pollution. If, in the same case, the buyer would prefer to terminate the contract on the basis of a fundamental breach by the seller and grants the seller an additional deadline for removal of the pollution, the final outcome of the case would still be the same: the seller must transfer the immovable free of any pollution. On the basis of this reasoning, priority of termination over avoidance is unnecessary because the seller’s rectifying the lack of conformity after its discovery excludes both options, terminating and avoiding the contract, for the buyer.

Notice of termination must be provided within reasonable time after a party to the contract has become or must have become aware of a fundamental breach of the contract (LOA § 118 (1) 1)) or after passing of the previously described additional deadline granted in accordance with the LOA’s § 114. Similar regulation of the deadline for notice of termination can be found in the PICC’s Article 7.3.2 (2), in the DCFR’s III.–3:508 (2), and also according to Article 49 (2) (b) of the CISG in the cases in which the seller has already delivered the goods to the buyer. The CISG’s Article 49 (1) regulates termination in a situation wherein the delivery has not occurred; in such a case, termination must occur either during the limitation period or by the deadline provided for in national law. Therefore, under Article 49 (1), termination is possible over rather a lengthy period of time.^{*59}

As mentioned above, the determination of a reasonable deadline depends on the various factors listed in § 7 of the LOA and, accordingly, may be rather different for different contracts. One finds in official commentaries to the PICC^{*60}, for example, that termination within reasonable time may mean immediate or prompt termination

⁵⁵ Münchener Kommentar/Kramer (Note 53), § 119, margin number 33.

⁵⁶ A sample list of fundamental breaches of contract is provided in § 116 (2). See Note 19.

⁵⁷ M. A. Simovart (Note 25), pp. 65, 70.

⁵⁸ CCSCd 3-2-1-44-04.

⁵⁹ U. Magnus (Note 47), p. 429.

⁶⁰ Available at <http://www.unilex.info/dynasite.cfm?dssid=2377&dsmid=13635>.

if a party is able to easily enter into a substitute transaction; where the possibility of a substitute transaction needs to be investigated, what constitutes reasonable time before the deadline is deemed to be longer. According to the commentaries to the Estonian LOA, a **reasonable** deadline cannot, as a rule, be construed as immediate or prompt notification and must, as a rule, in addition to searching for other options, take into account the time needed to become aware of the breach and weigh one's options (e.g., involving a lawyer).^{*61}

The main factors affecting the amount of time for a reasonable deadline for termination in application of the CISG's Article 49 (2) (b) are the nature of the goods that are the object of the contract and the other facts of the case.^{*62} Court practice reflects the position that the term for termination on grounds of fundamental breach starts at the moment when the buyer becomes aware of the **fundamental** nature of the breach and not the moment when the breach actually began.^{*63} We present here some examples from court cases in which Article 49 was applied: notice of termination given after five months^{*64}, eight months^{*65}, or three years^{*66} from one's becoming aware of a fundamental breach does not constitute notice within reasonable time; by contrast, one day^{*67}, 48 hours^{*68}, approximately 2.5 months^{*69}, and also three months^{*70} after discovery of a fundamental breach have been deemed to constitute a reasonable period for giving notice of termination. What is important here is that the reasonableness of the deadline is in any case dependent on the specifics of the case in question^{*71}, although a reasonable deadline is generally shorter rather than longer, usually being a couple of months at most.^{*72} German law, however, ties the deadline for exercising one's right of termination to the general limitation period applicable for claims (BGB §§ 218 and 323).^{*73}

The third reason German legal practice has treated contractual legal remedy (i.e., termination) as primary where there is competition between termination and avoidance is the short limitation period applicable for claims related to lack of conformity (up to six months before the BGB was reformed), which protects the seller and which should not be suppressed by the right of avoidance arising out of the BGB's § 119 (2). In the post-reform BGB and following introduction of changes to the regulation of the limitation period (BGB § 438), the issue of the deadline is no longer relevant in the context of protection of the rights of the seller.^{*74} Different countries employ rather different periods for giving notice of avoidance.^{*75} Pursuant to the BGB's § 121, notice of avoidance is to be given, without wrongful delay, from the moment when the party entitled to avoidance becomes aware of the basis for avoidance, while in German judicial practice promptly given notice has been understood to be notice given within two weeks after discovery of breach.^{*76} Under Swiss law, a person entitled to avoidance has one year after finding out about a mistake to give notice of avoidance (see Part 5 of the Swiss Civil Code: Article 31 of the obligation law (OR)^{*77}), and that time is three years under Austrian law (Article 1487 of the Austrian Civil Code^{*78}) and, in Holland, three years after discovery of a mistake (BW Article 52 (1)). Pursuant to DCFR II.-7:210, notice of avoidance has no legal effect unless given within reasonable time, with due regard to the circumstances, after the avoiding party knew or could reasonably be expected to have known of the relevant facts.

Under Estonian law, preference for termination over avoidance based on deadline is irrelevant, as the deadlines set for the exercise of the rights of termination and avoidance are, as a rule, not dramatically different temporally. As mentioned above, the right of termination ends upon a reasonable period of time having elapsed from

⁶¹ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 413.

⁶² R. Koch. Commentary on Whether the UNIDROIT Principles of International Commercial Contracts May Be Used to Interpret or Supplement Articles 47 and 49 of the CISG. December 2004. Available at <http://www.cisg.law.pace.edu/cisg/principles/uni47,49.html#rkiii>; U. Magnus (Note 47), p. 428.

⁶³ Italy, 13 December 2001, District Court Busto Arsizio (Machinery case). Available at <http://cisgw3.law.pace.edu/cases/011213i3.html>.

⁶⁴ Germany, 15 February 1995, Supreme Court (Key press machine). Available at <http://cisgw3.law.pace.edu/cases/950215g1.html>.

⁶⁵ France, 14 June 2001, Appellate Court Paris (*Aluminium and Light Industries Company v. Saint Bernard Miroiterie Vitrierie*). Available at <http://cisgw3.law.pace.edu/cases/010614f1.html>.

⁶⁶ Finland, 12 April 2002, Turku Court of Appeal (Forestry equipment case). Available at <http://cisgw3.law.pace.edu/cases/020412f5.html>.

⁶⁷ Germany, 17 September 1991, Appellate Court Frankfurt (Shoes case). Available at <http://cisgw3.law.pace.edu/cases/910917g1.html>.

⁶⁸ Spain, 3 November 1997, Appellate Court Barcelona (Rolled steel case). Available at <http://cisgw3.law.pace.edu/cases/971103s4.html>.

⁶⁹ Canada, 20 September 2002, Court of Queen's Bench of Manitoba (*Brown & Root v. Aerotech*). Available at <http://cisgw3.law.pace.edu/cases/020920c4.html>.

⁷⁰ Germany, 22 August 2002, District Court Freiburg (Automobile case). Available at <http://cisgw3.law.pace.edu/cases/020822g1.html>.

⁷¹ L. A. DiMatteo *et al.* (Note 46), p. 406.

⁷² "In this kind of commercial transaction, a reasonable time for notice is most often very short, at most a few months. To extend this period would require pressing circumstances indeed." HO Turku, 12 April 2002.

⁷³ Palandt. Bürgerliches Gesetzbuch. 65. Aufl. München 2006. C. Grüneberg § 323, comm. 33 (p. 526).

⁷⁴ K. Larenz, M. Wolf. Allgemeiner Teil des Bürgerlichen Rechts. München: C.H. Beck 2004, § 36, margin number 50 (p. 665).

⁷⁵ DCFR II.-7:210, Notes I-1, 2.

⁷⁶ Palandt. Bürgerliches Gesetzbuch. 65. Aufl. München, 2006. Helmut Heinrichs § 121, commentary 2 (p. 93).

⁷⁷ Adopted on 30 March 1911.

⁷⁸ Adopted on 1 June 1811.

the moment a party to the contract became or must have become aware of a fundamental breach of contract, while the right of avoidance expires six months after discovery of a mistake (GPCCA § 99 (1) 2)) but not later than three years after the entry into the transaction (GPCCA § 99 (2)).

In addition to the restriction based on the reasonableness of the deadline, Estonian law enables the party in breach to transform the notice of termination invalid in case the claim for the performance of the obligation has expired (LOA § 118 (2)). If the other party does not rely on the limitation period, termination is still possible, provided that the material prerequisites for termination exist. Pursuant to the GPCCA's § 146, the limitation period for a claim is, as a rule, three years (under subsection 1) and in exceptional cases it is either five (subsections 2 and 3) or 10 years (subsections 4 and 5) since the time the claim falls due (§ 147).

A notable situation concerns limitations of termination and avoidance of consumer sale contracts. Namely, in the case of consumer sale, the seller is, under § 218 (1) of the LOA, only liable for any lack of conformity of a thing if that non-conformity becomes evident within two years after the thing was delivered to the buyer. It is often the case with cars, home appliances, furniture, etc. that the buyer discovers the lack of conformity only after two years have passed since the receipt of the thing. There arises a question as to whether the buyer may terminate the contract on the basis of the existence of a relevant mistake under § 92 of the GPCCA in the case wherein more than two years have passed since the delivery of the thing but less than three years have elapsed since entry into the transaction^{*79} and the material elements necessary to constitute a mistake are present. Allowing this option would not be contrary to EU law, as, according to Article 8 (1) of the consumer sales directive^{*80}, the rights resulting from the directive are exercised without prejudice to other rights that the consumer may invoke under the national rules. Therefore, if national provisions foresee an alternative for avoiding a contract because of a mistake, such avoidance complies with the directive. The authors of this article consider that such an option should be permissible under Estonian law because avoidance of a contract of sale instead of termination would help — especially in cases like the one described above — to protect the buyers much more effectively, as compared to termination.^{*81}

To summarise, the duration of the option to terminate or avoid a contract of sale are regulated on different terms in Estonian law. Presumably, the reasonable time period for terminating a contract of sale is shorter than the time for avoiding a contract based on a mistake — although exceptions to this rule may be found. The regulation of the length of the period for avoidance on the basis of a mistake is subject to agreement by the contracting parties. However, agreement of parties as to the deadline for the right of termination does not automatically extend to the deadline for exercising the right of avoidance.

4. Effects of termination and of avoidance

The main difference between the consequences of termination and avoidance is that in the event of termination, the contract is terminated *ex nunc*, while in case of avoidance the contract becomes void since inception.^{*82} Termination creates a liquidation obligation including mutual reversal obligations (3-2-1-129-05) and, while the contractual obligations are in the main part terminated but not entirely, what clearly expire are the obligations directed at performance.^{*83} Termination normally does not terminate obligations *ex tunc*; instead, what was transferred is returned under a return obligation in compliance with the LOA's §§ 189–191. For instance, the parties will still be liable for the breaches that have occurred to date; agreements related to jurisdiction and arbitration, non-competition, and confidentiality clauses will continue to apply.^{*84} Similar principles can be found in DCFR III.–3:509.

However, with avoidance a contract becomes void; i.e., the legal basis for performing contractual obligations is lost. That which was received on the basis of an avoided transaction is to be returned pursuant to the provisions concerning unjust enrichment (GPCCA § 90 (2), the same in DCFR II.–7:303). Compared with termination, the duty to hand over is somewhat more restricted under the unjust enrichment provisions than those governing termination and only that must be handed over which actually made the recipient richer^{*85}, with, for

⁷⁹ Pursuant to GPCCA § 99 (2), a transaction shall not be avoided until after three years have passed from entry into the transaction.

⁸⁰ Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees. – OJ L 171, 7.07.1999, pp. 0012–0016.

⁸¹ As a marginal note, the authors would like to point out that with consumer sale contracts, the requirement under LOA's § 118 (1) that the buyer must terminate the contract within reasonable time period should not apply. Such a requirement is not included in the directive and the Member States are not allowed to establish consumer-related requirements in their national rules that would be stricter than the terms of the directive.

⁸² See also DCFR II.–7:212, Comments, A.

⁸³ P. Varul *et al.* Law of Obligations Act I (Note 5), p. 624.

⁸⁴ *Ibid.*, p. 625.

⁸⁵ *Ibid.*, p. 638.

example, his subjective intentions regarding the object of the contract taken into account (LOA § 1033 (1), as in DCFR VII.–6:101). However, in the case of a void mutual contract — including mutual contracts subject to avoidance⁸⁶ — one may appeal successfully to the lack of basis for enrichment only in the case where the contract is void because of the restricted active legal capacity of the recipient, or due to threats or violence on the part of the transferor (LOA § 1034 (1)). Thus, in the case of a contract of sale as a mutual contract being avoided on the basis of a mistake, it is not, as a rule, possible to rely on the lack of basis for enrichment and the buyer is required either to return the thing purchased or, if this is not possible, to compensate for the value of the thing, pursuant to the LOA's § 1032 (2). Likewise, the seller cannot rely on, for example, the fact that the money he received has been stolen from him and that thus he is not any richer by that amount. In this respect, the consequences of terminating or avoiding a contract of sale are largely overlapping.

Here the following difference may be observed: in the case of termination by the buyer, it is always possible to demand payment of interest on the transferred funds (LOA § 189 (1), 3rd sentence), while in the case of unjust enrichment (i.e., avoidance of the contract), this can be done only if the recipient knew or must have known at the time of transfer that the contract was avoidable (LOA § 1035 (1) and (3) 2), GPCCA § 91). Thus, if the seller was or must have been aware of a relevant mistake on the part of the buyer (GPCCA § 92 (3) 1) or 2)), the buyer has the right to demand payment of legal interest on the refunded money on the basis of the LOA's § 1035 (1) or (3) 2); however, if both parties made a mistake (*ibid.*, clause 3), the buyer does not have that right. But if both parties' fundamental mistake gives rise to termination, the buyer may in any case demand interest on the refunded purchase price, and from this angle it would be more beneficial to the buyer to terminate and not avoid the contract.

Claims for compensation of damage are also different with termination and avoidance. In the case of avoidance, the buyer has just a negative claim for compensation (reliance measure); that is, he may demand to be put in the position he would have been in if he had not entered into the transaction (GPCCA § 101, also DCFR II.–7:304). With termination, however, the buyer has a positive right to claim compensation (expectation measure); i.e., he may demand to be put in the position that he would have had if the contract had been properly performed (LOA § 115, with the same principle being mirrored in DCFR III.–3:509).

To sum up, in cases where the seller is in fundamental breach of contract, as far as the consequences of restitution are concerned, it is somewhat more beneficial for the buyer to terminate and not to avoid the contract. Primarily this holds true to the extent of the buyer's potential claim for compensation and, in part, also to the claim for payment of interest. On the other hand, the buyer should be aware that, with termination, the seller will continue to have the right to make a claim for compensation or contractual penalty against the buyer.

5. Conclusions

Having examined possible cases of overlaps of termination and avoidance, it becomes clear that such overlaps are indeed possible. Since the deadlines for giving notice of termination and avoidance are subject to different regulation, the time periods for exercising the two alternative options might not necessarily be identical: although under Estonian law the entitled person normally retains the right of avoidance over a longer period than is seen with termination, the opposite may hold true exceptionally and in view of the facts of specific cases. Also, legal consequences of termination and avoidance are not the same: the two significant differences are that it is not always possible to demand payment of interest on the amounts refunded on the basis of the avoidance and unjust enrichment provisions, although this can be done with termination. In the case of termination, the parties will continue to have to perform certain requirements and obligations arising out of the previous performance of the contract.

Taking into account the general principles of private law — the principles of good faith and private autonomy, including freedom of contract — the authors of this article are not proponents of restricting the freedom of an individual to choose between these two institutions. The regulation provided in the DCFR is generally justified, and in Estonian law as well we should observe the principle that where circumstances of fact arise enabling a person to choose either to terminate or avoid a contract, the person is free to choose the remedy he prefers.

At the same time, the regulation of the deadline for avoidance of contract for mistake should be treated as dispositive, and in this respect the parties may themselves restrict their freedom of choice. If it is not obvious which remedy (termination or avoidance) a person is employing, that person's declaration of intent should be interpreted in the way most favourable to him.

⁸⁶ T. Tampuu. Lepinguväliste võlasuhete õigus (Non-contractual Obligations Law). Tallinn: Juura 2007, p. 102 (in Estonian).



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On Imperative Regulation of Information Duties in Financial Services Contracts

The principle of freedom of contract is the main principle of harmonised European contract law.^{*1} Although a contract creates only relative legal relations (i.e., legal relations between the parties to the contract), it may also concern interests requiring protection of the interests of third persons. The freedom of contract should be restricted where the background of its impact is not compatible with the regime of individual rights.^{*2} Modernisation processes — first and foremost, the evolution of the ‘cyber’ world — and, at the same time, dramatic change in the security situation of society in the wake of 11 September 2001 and the acts of terror that followed, and the crisis of the financial markets that began in 2007, have forced Europe to cherish more the security of society and sustainable development of the economy.^{*3} At a time of formation of a ‘risk society’, one cannot but support the position of Professor M. R. Marella that the general principle of human dignity set forth in Article 1 of the Charter of Fundamental Rights of the European Union should be seen as a potential source for new restrictions of the freedom of contract under European law.^{*4} National, supranational, and international imperative legislative or regulatory provisions of public law may affect the validity of a contract — a principle taken into account in Article 15:102 of the Principles of European Contract Law^{*5} (PECL). Article 15:101 of the PECL provides that a contract is of no effect to the extent that it is contrary to principles recognised as fundamental in the laws of the Member States of the European Union. Essentially the same idea is expressed as a key value in the Draft Common Frame of Reference (DCFR), prepared by the Study Group on a European Civil Code and the Acquis Group, which was presented to the Commission of the European Communities on 28 December 2007.^{*6}

In the information society, which is a product of the modernisation process, most of the values created by mankind are contained in information. In modern society, information is increasingly found to be a subject

¹ J. W. Rutgers. An Optional Instrument and Social Dumping. — *European Review of Contract Law* 2006 (2) 2, pp. 198.

² R. Brownsword. *Contract Law Themes for the Twenty-First Century*. Oxford University Press 2006, pp. 65.

³ See Article 2 (2) and (3) of the Treaty of Lisbon, which amended the Treaty on European Union and the Treaty establishing the European Community. — OJ C 306, 17.12.2007, p. 10.

⁴ M. R. Marella. The Old and the New Limits to Freedom of Contract in Europe. — *European Review of Contract Law* 2006 (2) 2, p. 274.

⁵ The Principles of European Contract Law. Parts I (1995, 1999) and II (1999). O. Lando, H. Beale (eds.). The Hague 2000; Part III. O. Lando, E. Clive, A. Prüm, R. Zimmermann (eds.). The Hague 2003. See also O. Lando. The European Principles in an Integrated World. — *European Review of Contract Law* 2005 (1) 1, p. 18.

⁶ C. von Bar, E. Clive, H. Schulte-Nölke (eds.). *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference. Interim Outline Edition*. München: Sellier 2008, p. 18. Available at <http://www.law-net.eu/> (27.11.2008).

of legal regulation: its prerequisites, consequences, content, and form may all be subject to regulation.^{*7} The amount of information disclosed in pre-contractual negotiations is closely linked to business ethics and the prevailing practices in the concrete locality and area of activity, and it is complemented by the impacts of a society that pursues specialisation. In this age, information duties are a sensitive legal-political issue. One can find opposing treatments of this particular obligation in the legal literature. Some approaches rely more on the general principles of the freedom of contract; others take a position contrary to freedom of contract.^{*8}

The problems related to provision of information are extensive and multifaceted in the case of financial services contracts. Promotion of security, sustainability, and general reliability of commerce is what contract law provisions should ensure, and, to this end, an *ex ante* approach must be guaranteed with contractual relations in financial services. Because of the limited scope of this article, it focuses on the specifics of the problems surrounding the information duties in entering into financial services contracts. It also discusses the imperative regulations with regard to notification applicable to financial services contracts under current Estonian law as part of the aftermath of the changing security situation in society. The security of society is a prerequisite for the preservation of human dignity, thus outweighing other values. The author considers to what extent the legislator has, in order to protect this prevailing public interest, imposed on the credit and financial institutions the obligation to gather information on customers. For the purposes of this article, the term 'financial services contracts' refers to contracts for provision of investment services and services allowed to management companies, as well as services specified in § 6 (1) of the Credit Institutions Act (CIA)^{*9} and insurance contracts.

1. General justifications for mandating special provisions for information duties

1.1. Positions of the market failure thesis

Modern legal provisions concerning the financial market are largely based on the market failure thesis. This theory proceeds from the premise that an unregulated market is the norm and regulation is necessary only when well motivated, in cases of special cause. According to the thesis, the role of the government in the economy is negligible and the market in its natural state must be restored. However, the market is not ideal and markets may collapse.^{*10} Regulation is necessary where the private sector may cause collapse of the markets or other sub-optimal consequences.^{*11}

One of the central premises of that theory is that any establishment of imperative regulation of information needs to be justified. According to the prevailing viewpoint, financial markets are incapable of giving investors information that would be at the socially optimal level. It is becoming increasingly difficult for an individual to understand, with financial services contracts, the economic benefit of the contract or to choose a proper goal — i.e., to furnish, upon entering into the contract, for themselves the objective criteria for reasonability. The options provided in contract law for solving the problem of asymmetry are considered to be insufficient.^{*12} Upon the use of financial services, especially in the case of long-term contracts, two problems exist simultaneously:

- 1) the problem of availability of information (i.e., asymmetric information) and
- 2) the problem of comprehensibility of information and that of the ability to use information.

1.1.1. Availability of information (information asymmetry)

In specialist literature, financial services are often referred to as products of trust, because their actual benefits will not usually be clear until much later, well after the contract is signed^{*13}, or as intangible and abstract legal

⁷ E. Tikk, A. Nõmper. *Informatsioon ja õigus* (Information and Law). Tallinn: Advokaadibüroo Raidla Partnerid, Juura 2007, pp. 18–19 (in Estonian).

⁸ See T. Wilhelmsson, C. Twigg-Flesner. Pre-contractual information duties in the *acquis communautaire*. – *European Review of Contract Law* 2006/4, p. 446.

⁹ *Krediidiastutuste seadus*. – RT I 1999, 23, 349; 2008, 3, 21 (in Estonian); available in English at <http://www.just.ee/23295> (version dated 1.01.2007).

¹⁰ R. Cooter, T. Ulen. *Law and Economics*. 4th edition. Boston: Pearson, Addison Wesley 2004, pp. 205–206.

¹¹ C. Goodhart, P. Hartmann, D. Llewellyn, L. Rojas-Suarez, S. Weibrod. *Financial Regulation: Why, How and Where Now?* London: Routledge 1998, pp. 4–8.

¹² H. Mcvea. *Financial Services Regulation. Under the Financial Services Authority: A Reassertation of the Market Failure Thesis*. – *The Cambridge Law Journal* 2005, pp. 421–422.

¹³ P. Cartwright. *Banks, Consumers and Regulation*. Hart Publishing 2004, p. 51.

products that are defined in the terms of contract such that generally it is difficult to estimate the mutual rights and obligations of the parties or to evaluate, in detail, the price-to-quality ratio.^{*14}

In the case of using a financial service under a long-term contract, often problems are encountered that are related to the timeliness and reliability of the information available to the parties. On the one hand, the information available to a service provider regarding the customers and their needs changes. Information is of paramount importance for enterprises in the financial sector in their everyday practice in evaluating risks^{*15} and making management decisions.^{*16} According to the new regulation on the adequacy of the banks' capital, the amount and quality of information have a direct effect on the calculation of capital requirements.^{*17} Therefore, the economic value of information, including information on the person of the customer, changes over time and the provider of the service wants, at all times, more information on the customer.

On the other hand, over time the actual value becomes less and less transparent for the customer.^{*18} It is difficult and costly for the customer to obtain relevant information about the financial services because collecting information on the usefulness of a service requires specific knowledge about the realm of financial risks. In using services, especially those provided over the Internet, investors have at their disposal many different sources in addition to the information disclosed to them by the contract partner. Those other sources include the information disclosed by enterprises providing services of advising about financial information and related consultancy services and that are not subject to regulation under public law. The legal regulation of advising and consultation focuses more on the methods of providing traditional financial services.^{*19} Overabundance of available information does not necessarily ensure reasonable decision-making, as it makes it more difficult to evaluate the existing information.

1.1.2. Comprehensibility of information and ability to use information

The problem of comprehensibility of information and the ability to use it may, in other words, be treated also as a problem of forming a declaration of intention. In the realm of financial services there is a huge difference between the objective content of reasonableness and the ability of a person to rationally weigh his decisions. A customer does not necessarily know which kind of information would aid his decision-making, and, from his existing experience, the customer is incapable of foreseeing future development trends.

The customer's ability to understand and use information and to act on the basis of the available information is cognitively restricted. People behave in line with their perceptions, prejudices, inclinations, and other so-called 'show of fingers' rules. Studies show that people's outlook for the future is often unrealistically optimistic.^{*20} Unrealistic estimation of one's actions and outlooks bring about transactions wherein contractual justice is not guaranteed. The real price of such transactions and incidental risks will, in aggregate, start having a negative effect on financial markets. Contracts entered into as a result of bad decisions may result in ineffective investments, which affect the financial market as a whole and, from the point of view of society, represent waste of means. Bad financial decisions, including over-borrowing, are associated with failure to give sufficient information in the pre-contractual negotiations stage.^{*21}

Individuals who are capable of estimating financial information contribute to effective functioning of the financial markets. They sense the risks of different financial services better. As the financial markets become

¹⁴ M. Ebers. Information and Advising Requirements in the Financial Services Sector: Principles and Peculiarities in EC Law. – Electronic Journal of Comparative Law, June 2004 (8.2). Available at <http://www.ejcl.org/82/abs82-2.html> (20.03.2008).

¹⁵ According to the general approach, risk means the danger of wrong decisions, i.e., the danger that the chosen goal is not achieved in full or at all; the risk inherent in making a decision always is due to the uncertainty of the consequences of such a decision.

¹⁶ O. Karma, T. Paas. Riski mõiste ja majandusriskid – Riskid Eesti majanduses (The Concept of Risk and Economic Risks — Risks in Estonian Economy). Tartu: Tartu Ülikooli Kirjastus 2000, pp. 51–53.

¹⁷ A new international standard, known as Basel II, is transposed into European law with Directives 2006/48/EC and 2006/49/EC. Corresponding changes in the Estonian Credit Institutions entered into force on 1 January 2007. For instance, § 8616 (1) establishes that "The less information is at the disposal of a credit institution, the more conservative the credit institution shall be in designation of ratings to the debtors and transactions."

¹⁸ Due to the risks related to exchange rate fluctuations, stock exchange listing or the stock exchange index and other risks inherent of the financial market, the solvency and general financial soundness of the service provider, the quality of the service, variable rate interest and the related service charges — they all change. The legislator accepts the impact of the market situation also in the regulation of general conditions for providing financial services in conformity with clause 2 of the Annex of the Council Directive 3/13/EEC of 5 April 1993 on unfair terms in consumer contracts, transposed into Estonian law by LOA § 43.

¹⁹ See D. Kingsford-Smith, K. Williamson. How Do On-line Investors Seek Information, and What Does This Mean For Regulation? – Electronic Law Journals. Journal of Information, Law and Technology 2004/2. Available at http://www2.warwick.ac.uk/fac/soc/law/elj/jilt/2004_2/kingsford-smithandwilliamson (28.04.2008).

²⁰ H. Mcvea (Note 12), p. 422. See also P. Cartwright (Note 13), p. 55.

²¹ Questionnaire for the Attention of the Government Expert Group on Mortgage Credit. Letter of the Commission of the European Communities, dated 1 April 2008, No. MARKT/H3/CH D (2008).

increasingly complicated and consumers are expected to demonstrate greater responsibility and risk-tolerance in making decisions, individuals' awareness is necessary not only for their own welfare but also to facilitate smooth functioning of the financial markets.^{*22} On the basis of the above, one can conclude that the information disclosed upon entry into financial services contracts and the comprehensibility of that information in forming the intention of the parties to the contract have a great impact both on the contractual parties and on society as a whole.

1.2. Differences due to the specific role of banking

In modern society, finance has a special role in every country's economy. The main purpose in regulating the credit institutions is to ensure a functioning banking system.^{*23}

Here we should remember the position of Anthony Giddens that, in modernity, most of our material and social life is organised by abstract expert systems. Expert systems are understood by Giddens to be primarily technological systems that tie local practices to global relations, and according to him we understand someone else's competencies in distanced time and space. Reliance on expert systems often does not assume any personal contact with the individuals or institutions that, figuratively speaking, are responsible for such expert systems.^{*24}

Readiness to trust expert systems is of key importance in the case of transactions over the Internet or via other means of communication, and also in electronic banking, insofar as such innovative practices assume that a technically advanced and abstract system is trusted and occur disembedded from time and space.

Banks and other providers of payment services take the role of an expert system in today's commerce; trusting their competence and technological systems ensures for other parties a reliable option of performing monetary obligations by using non-cash payment methods. Today, the risk of non-performance of a monetary obligation lies primarily with the banks — i.e., a specialised mediator who is capable of minimising risks at the lowest cost.^{*25}

Because of the special role discussed above, the legislator has imposed certain obligations in public law on the banks and other providers of payment services whose purpose is to increase the reliability of commerce and society as a whole.

2. Purposes of information duties upon entry into a financial services contract and types of information

2.1. Justification of special provisions for financial services

The legal literature approaches the purposes and functions of information duties in contractual relations from different angles. According to the approach generally adopted in Estonian legal literature, what is differentiated is the general protection obligation expected from the individuals engaged in pre-contractual negotiations — the parties are required to take into account reasonably each others' interests and rights, meaning that they are required to consider the circumstances^{*26} set out in § 7 (2) of the Law of Obligations Act^{*27} (LOA) in estimating the behaviour of the other negotiating party and to disclose accurate information during preparations for the signing of the contract.^{*28}

²² Improving Financial Literacy. Analysis of Issues and Policies. OECD Publishing 2005, p. 20.

²³ See H. Kumpel. Bank- und Kapitalmarktrecht. 2. Aufl. Köln 2000, p. 16.

²⁴ A. Giddens. The Consequences of Modernity. Stanford: Stanford University Press 1990, p. 27.

²⁵ A. de Jasay. The Failure of Market Failure: Part I. The Problem of Contract Enforcement. The Library of Economics and Liberty. Available at <http://www.econlib.org/library/Columns/y2006/Jasayfailure.html> (15.05.2008).

²⁶ LOA § 7 (2): In assessing what is reasonable, the nature of the obligation, the purpose of the transaction, the usages and practices in the fields of activity or professions involved and other circumstances shall be taken into account.

²⁷ Võlaõigusseadus. – RT I 2001, 81, 487; 2007, 56, 375 (in Estonian).

²⁸ P. Varul, I. Kull, V. Kõve, M. Käerdi (compilers). Võlaõigusseadus. Üldosa (§§ 1–207). Kommenteeritud väljaanne (Law of Obligations Act. General Part (§§ 1–207). Commented edition). Tallinn: Juura 2006, § 14 commentary 3 (in Estonian).

European law proceeds in its regulation of financial services contracts from the specific nature of the service. The Commission of the European Communities is of the position that the regulation of pre-contractual information duties for consumer protection purposes should focus on certain sectors (insurance contracts law and financial services).^{*29} Regulation of information duties is also prominent in the most recent directives concerning the financial market, adopted between 2005 and 2007.^{*30}

The legal regulation of information duties in financial services and disclosure of the activities of enterprises is intended to ensure regular and effective functioning of the market. M. Ebers finds that, as far as financial services are concerned, in European law information duties have become rooted in connection with consumer protection or the method of concluding a transaction. Information duties within financial services have been deemed important in European law irrespective of whether the customer is a consumer (in a 'B2C' transaction) or a person participating in economic and professional activities (in the 'B2B' case). This holds true, for instance, for cross-border payments, transactions in securities, and insurance contracts.^{*31}

In the conditions of a global financial market, the problems specific to the security of services provided by electronic means of communication have become more acute. The 'cyber' world encourages anonymity; the identity of persons has widened and freedom has taken purchase of a new content. The Internet increases the risks of taking advantage of and damaging consumers, even if we think that unfair terms of contract are not a new problem *per se*. The problems of unfair terms of contract, and also those of consumer protection, coincide with the same problems in the cyber world — cyber crime. This interferes with the functioning of the market, and whether a B2B or B2C relationship is involved, or some other kind, is not important.^{*32} The cyber world is made up of organising elements — information — and may by its nature be anarchistic. The anarchistic nature of the cyber world becomes understandable if we differentiate organisation from regulation in the same way we differentiate a provision from a rule. Professor R. Polcak has even adopted the viewpoint that traditional legal conceptions are useless for the cyber world, and that conceptions different from those based on the threat of the state's coercive powers must be found.^{*33}

The author of this article supports the positions of the market failure thesis (see section 1.1 of this article) and Professor M. Ebers in that the regulation of information duties upon entry into financial services contracts is not so much tied to consumer protection as due to the specific nature of financial services and to the purpose of keeping all investors sufficiently informed that they are able to make rational decisions. There are peculiarities in the financial sector, with such contracts being noticeably more complicated than normal purchase and sale agreements, and any problems related to overabundance of information are resolved differently from those found under other types of contract.^{*34}

From the above reasoning, it is not justifiable for legal literature to consider information duties in financial services contracts and other contracts for goods and services without drawing a clear distinction between them.

2.2. Information disclosed for the purpose of protecting public interests

The extent of information duties and the content of information are greatly affected by market conduct rules; also other restrictions are applicable to the reliability of the activities of providers of financial services. We will proceed to treat just one aspect of these: legal provisions concerning prevention of money laundering and financing of terrorism.

The content and amount of information disclosed during pre-contractual negotiations for entry into a long-term contract for financial services are to a large extent determined by the legal provisions concerning prevention of money laundering and terrorism. The battle against money laundering and even more the efforts to suppress terrorist financing have an international dimension — the obligations of countries in this respect arise out of several international conventions^{*35} and related international

²⁹ Commission of the European Communities. Second Progress Report on the Common Frame of Reference. Brussels, 25.07.2007. COM(2007)447 final. Available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2007:0447:FIN:EN:PDF> (27.11.2008).

³⁰ S. Grundmann, J. Hollering. EC Financial Services and Contract Law – Developments 2005–2007. Report. – European Review of Contract Law 2008 (1), pp. 45–64.

³¹ M. Ebers (Note 14).

³² G. Decocq. Cyber Consumer Protection and Unfair Competition. – Electronic Journal of Comparative Law, December 2007 (11.3). Available at <http://www.ejcl.org/113/article113-18.pdf> (23.04.2008).

³³ R. Polcak. In Law, We Trust: Shortly to Bumblebees and the Normativity of Law in Cyberspace. Conference paper Cyberspace 2005, Conference organised by Masaryk University, Faculty of Law with School of Social Studies 7–8 November 2005, Masaryk University, p. 7.

³⁴ M. Ebers (Note 14). See also H. Mcvea (Note 12), p. 421.

³⁵ See W. C. Gilmore. Dirty Money. The Evolution of International Measures to Counter Money Laundering and the Financing of Terrorism. Council of Europe Publishing 2004, p. 65–77. Estonia has acceded to the Vienna Convention (RT II 2000, 15, 926), Strasbourg Convention (RT

standards.^{*36} Money laundering is capable of damaging the stability of each and any credit institution and the integrity of the entire financial system of a country, thus causing significant financial damage. Recital 1 of the preamble to Directive 2005/60/EC on prevention of the use of the financial system for the purpose of money laundering and terrorist financing^{*37} sets forth that, in addition to the criminal law approach, a preventive effort via the financial system can produce results. Providers of financial services are required to apply risk-based due-diligence^{*38} procedures to address money laundering and financing of terrorism not to combat crime but in order to protect the integrity of credit and financing institutions and the entire financial system.^{*39} In this day and age, combating money laundering is viewed as a part of monetary policy.^{*40}

For instance, on 21 September 2001, the European Council stressed that combating terrorism was one of the main goals of the European Union. In their daily operations, providers of financial services are required to apply international sanctions established by UN resolutions and the regulations issued within the framework of the common foreign and security policy of the European Union. Insofar as UN resolutions are not directly applicable in national legal systems, the providers of financial services operating in Estonia must also adhere to the orders of the Government of the Republic issued by the Government of the Republic on the basis of the International Sanctions Act.^{*41} Sanctions may be applied to the governments, associations, and individuals of third countries. Financial sanctions may be used to restrict movement of payments, granting of (export) credit, making of investments, disposal of related funds, etc.^{*42}

Because of the threats posed by the crimes of money laundering and terrorism, prevention of such crimes may be treated as serving **prevailing public interest**, which gives the public authorities sufficient grounds to impose obligations on persons and restrict the rights of persons^{*43}, *inter alia*, to restrict the freedom of contract and to imperatively regulate information duties in the course of pre-contractual negotiations.

Therefore, one should not accept R. Zimmermann's position that obligations related to information disclosure and counselling belong solely to the realm of contract law and all the associated problems should be discussed in that context.^{*44}

2.3. Types of information disclosed upon entry into a financial services contract

The legal literature's treatment of the purposes of information disclosed upon entry into financial services contracts and of the types of such information generally focuses on the types of information disclosed for the purposes of consumer protection. M. Ebers, for instance, distinguishes among information about the supplier, the financial service, certain forms of distribution, and legal remedies.^{*45} P. Cartwright distinguishes among information about the service, institutional information of the service provider, information about the rights guaranteed by law, and financial education.^{*46} H. Herrmann employs distinction among information given in responding to specific questions asked by the customer or in reporting to the customer, giving explanations to or counselling the customer, issuing warnings, and making enquiries.^{*47}

II 2000, 7, 41), Palermo Convention (RT II 2003, 1, 1) and UN 1999 International Convention for the Suppression of the Financing of Terrorism (RT II 2002, 12, 45).

³⁶ The national provisions concerning the prevention of money laundering and terrorist financing must take into account the 40 recommendations and nine special recommendations against the financing of terrorism of the Financial Action Task Force, FATF (available at <http://fatf-gafi.org>). These recommendations represent one of the twelve standards of stable financial environment (<http://www.fsforum.org>) and they were also the basis from which Directive 2005/60/EC was developed.

³⁷ OJ L 309, 25/11/2005, pp. 0015–0036.

³⁸ The concept of 'due diligence' is provided for in § 13 of the Prevention of Money Laundering and Financing of Terrorism Act.

³⁹ See W. C. Gilmore (Note 35), pp. 93–97.

⁴⁰ I. Tibar. Rahapesu kujunemisloost ja olemusest (On the Evolution and Nature of Money Laundering). – Juridica 2007/8, p. 578 (in Estonian).

⁴¹ Rahvusvahelise sanktsiooni seadus. – RT I 2002, 105, 612; 2004, 2, 7 (in Estonian).

⁴² Application of International Sanctions within the Framework of the Common Foreign and Security Policy of the EU. Available at http://ec.europa.eu/external_relations/cfsp/sanctions/index_et_2006.pdf (22.04.2008).

⁴³ Seletuskiri rahapesu ja terrorismi rahastamise tõkestamise seaduse juurde (137 SE) (Explanatory Memorandum to the Money Laundering and Terrorist Financing Prevention Act (137 SE)). Available at http://www.riigikogu.ee/?page=en_vaade&op=ems&eid=163492&u=20080716212957 (27.11.2008).

⁴⁴ R. Zimmermann. The New German Law of Obligations. Historical and Comparative Perspective. Oxford University Press 2005, p. 212.

⁴⁵ M. Ebers (Note 14).

⁴⁶ P. Cartwright (Note 13), p. 56.

⁴⁷ H. Herrmann. Bank–Customer Relationship in German Law and Practice. – German Banking Law and Practice in International Perspective. N. Horn (ed.). Berlin, New York: Walter de Gruyter 1999, p. 99.

The author believes that the above-mentioned approaches do not exhaust all of the important types of information. They do not take into account the customer's obligation to give to the financial services provider information necessary for the latter to meet the obligations imposed in public interests. Indubitably, the service provider has identifiable essential interest in such information. This issue cannot be approached solely on the basis of the relevant provisions of contract law.

After analysing different legal provisions, one is justified in distinguishing among the following information types with respect to the parties' information duties for the purpose of financial services contracts — i.e., information about:

- the service provider;
- the person of the recipient of the service, including the customer's financial expertise, risk-tolerance, and solvency, and other information necessary for applying the 'know your customer' principle;
- the content of the service;
- the service charges and interest rates;
- the security requirements of the service, including those pertaining to account-blocking and the principles applied in processing of the customer's personal data;
- the deposit and investment guarantee schemes;
- the options for settling disagreements between the parties; and
- the options for termination of the contract.

2.4. Information about the person of the recipient of the service

Whether or not anti-money-laundering or anti-terrorism due-diligence methods can be applied depends largely on the personal and other information received from the customer in the course of concluding a settlement contract or a long-term contract for the use of other financial services. In conclusion of a settlement contract or other long-term contract entailing rights of account, it is paramount that the service provider meet the obligation, in conformity with the principle of the formal right of account, to ascertain the identity of the person declaring intention to enter into the contract, and to validate such information. A bank must verify the real name and identify of the customer and be sure that the customer is not using a false name. Pursuant to § 89 (2)¹ of the Estonian Credit Institutions Act, upon entry into a contract or transaction, the credit institution is required to identify the customer or the representative thereof.

These days in Europe, the positions and practices of theorists are largely influenced^{*48} by the Basel Committee on Banking Supervision guidelines 'Customer Due Diligence for Banks'^{*49} and its annex 'General Guide to Account Opening and Customer Identification'.^{*50} Because of the regulative arbitrage argument, it is of utmost importance that the content and extent of the information disclosed by the customer upon entry into a financial services contract be similarly regulated by law in the countries in the same region.

In Estonia, the requirements concerning the identification and verification of the customer's identity are regulated in the general terms and conditions of every credit institution and are specified in the standard terms of their settlement contracts. The information a credit institution is required to obtain from a customer during pre-contractual negotiations is not determined by the Law of Obligations Act. It arises from other legislation. The requirements for the documents and other information to be provided during pre-contractual negotiations are also laid down in the internal provisions of credit institutions; such internal provisions must comply with Ministry of Finance Regulation 10 of 3 April 2008 on 'Requirements for the Rules of Procedure Established by Credit and Financial Institutions, for the Application and Control of Implementation of Such Rules'.^{*51}

Next we shall look at the legal provisions to which a financial services provider must adhere in Estonia in obtaining information about the customer during pre-contractual negotiations.

The Money Laundering and Terrorist Financing Prevention Act^{*52} (MLTFPA) specifies the information necessary for application of due-diligence measures. Pursuant to MLTFPA §§ 12 and 13, which are based on articles 7 and 8 of Directive 2005/60/EC and the 5th recommendation of the Financial Action Task Force

⁴⁸ See, e.g., *Otmyvanye deneg. Bankovskii monitoring. Hypo Investment Bank (Liechtenstein) (ed.). Gratz: NWV Neuer Wissenschaftlicher Verlag 2006. See also W. C. Gilmore (Note 35), p. 108.*

⁴⁹ *Customer Due Diligence for Banks. Basel Committee on Banking Supervision. Publication No. 85. Available at <http://www.bis.org/publ/bcb85.htm> (28.04.2008).*

⁵⁰ *General Guide to Account Opening and Customer Identification. Basel Committee on Banking Supervision. Publication No. 85. Annex. Available at <http://www.bis.org/publ/bcb85annex.htm> (28.04.2008).*

⁵¹ *Nõuded krediidi- ja finantseerimisasutuse poolt kehtestatavatele protseduurireeglitele ning nende rakendamisele ja täitmise kontrollimisele. – RTL 2008, 29, 428 (in Estonian).*

⁵² *Rahapesu ja terrorismi rahastamise tõkestamise seadus. – RT I 2008, 3, 21; 2008, 27, 177 (in Estonian).*

(FATF)^{*53}, persons providing financial services are required to identify, upon concluding a long-term contract, each customer against the documents and data submitted by the customer and verify said information on the basis of information from a reliable and independent source, and also to identify and verify the identity and representation rights of the representative of a natural or legal person. If so requested during pre-contractual negotiations, a customer must submit not only documents providing verification of identity and/or right of representation but also information on the beneficial owner^{*54}, on the purpose of the transaction, and on the source and origin of the funds to be used for the transaction. In identification of a beneficial owner, it is important for the credit institution to understand the circle of owners and shareholders, and the control structure of the legal person who participates in or is the customer in the transaction, and also to know who is actually in charge of the operations of the legal person and whose financial situation the transaction really affects, as well as who benefits from it. In conformity with MLTFPA § 23, upon entry into a settlement contract, the bank shall identify all natural persons on equal bases, irrespective of whether a person wants to open an account in his own name or acts as a representative of another natural or a legal person. The same principles have been adopted in Finland and Sweden, where such requirements arise from a standard or a guideline established by a supervisory authority.^{*55}

In Estonia, active information duties have been prescribed for the customer to be followed upon entry into long-term contracts pursuant to MLTFPA § 23 (4). During negotiations with a credit or financial institution, a customer has no right to remain silent about information the service provider needs for application of due-diligence measures. Such a legal provision induces creation of a trust-based contractual relationship between both parties and reduces to a minimum the risk of errors related to the identity of a customer. This represents a special provision of the customer's information duty and should ultimately support acting in good faith. The information duties of the customer arising out of the special provisions are significantly wider and more precise than is traditionally required in relative obligation relations. Therefore, one can conclude that the requirement of society's security and sustainability significantly extends protection obligations in contractual relations to those who are not actually party to the contract.

In applying financial sanctions, a credit institution is required to ascertain the full surname, first name(s), pseudonyms, sex, date and place of birth, nationality, citizenship, address (place of residence), and passport (ID card) identifier. Information necessary for identification is published in relevant lists. The course of identification must ensure that the provider of financial services can be sure that no international sanctions are applicable to the person wishing to enter into a contract.^{*56}

In addition to the aforesaid, a payment services provider needs to consider, during pre-contractual negotiations, regulation (EC) 1781/2006 of the European Parliament and of the Council of 15 November 2006 on information on the payer accompanying transfers of funds.^{*57} Complete traceability of money transfers may be especially important and valuable in prevention, investigation, and detection of money laundering or terrorism. To achieve this goal, payment service providers are required to communicate precise and concise information about the payer when making the transfer. Pursuant to Article 4 of the above-mentioned regulation, complete information on the payer shall consist of name, address, and account number. The address may be substituted for with the date and place of birth of the payer and his customer identification number or national identity number. Where the payer does not have an account number, the payment service provider of the payer shall replace this with a unique identifier that allows the transaction to be traced back to the payer. The payment service provider of the payer shall, before transferring the funds, verify the complete information on the payer on the basis of documents, data, or information obtained from a reliable and independent source. Therefore,

⁵³ Financial Action Task Force. The 40 Recommendations. Available at http://www.fatf-gafi.org/document/28/0,3343,en_32250379_3223693_0_33658140_1_1_1_1,00.html (30.04.2008).

⁵⁴ Pursuant to MLTFPA § 8, a beneficial owner is a natural person who, taking advantage of his or her influence, exercises final control and in whose interests or favour or on whose account a transaction or act is performed. A beneficial owner is also a natural person who has or exercises final control over management of a company by having over 25 percent of shares or voting rights through direct or indirect shareholding or control, including in the form of bearer shares; otherwise exercising control over management of a legal person. A beneficial owner is also a natural person who, to the extent of no less than 25 percent determined beforehand, is a beneficiary of a legal person or civil law partnership or another contractual legal arrangement, which administers or distributes property, or who exercises control over the property of a legal person, civil law partnership or another contractual legal arrangement to the extent of no less than 25 percent. A beneficial owner is also a natural person who, to an extent not determined beforehand, is a beneficiary of a legal person or civil law partnership or another contractual legal arrangement, which administers or distributes property, and in whose interests a legal person, civil law partnership or another contractual legal arrangement is set up or operates.

⁵⁵ Guidelines of the Swedish Finansinspektionen, 9 June 2005. Regulations and General Guidelines Governing Measures against Money Laundering and Financing of Particularly Serious Crimes in Certain Circumstances, § 8. Available at http://www.fi.se/Templates/SearchPage_1687.aspx?pattern=money+lauding; Standard 2.4 of the Finnish Rahoitustarkastus. Code of Conduct. Customer Identification and Customer Due Diligence, pp. 16 and 26. Available at http://www.fi.se/Templates/SearchPage_1687.aspx?pattern=money+lauding (1.05.2008).

⁵⁶ Council of the European Union. EU Best Practices for the effective implementation of restrictive measures, 14.06.2006. Available at <http://register.consilium.europa.eu/pdf/en/06/st10/st10533.en06.pdf> (22.04.2008).

⁵⁷ OJ L 345, 8.12.2006, pp. 0001–0009.

each person who submits a payment order to the credit institution (irrespective of whether that person has entered into a settlement contract) must be properly identified by the credit institution.

On the basis of the above discussion, it is clear that both the European and Estonian legislator consider it very important that credit and financial institutions gather precise information about the identity of their customers and have granted the financial services providers legal means to minimise the risk of making an error in the identification of the other party to the contract.^{*58} Credit and financial institutions can reduce the risks of not knowing the personal data of the customer in conformity with their general terms and conditions, standard terms, and internal provisions.

3. Conclusions

Nowadays, contract law carries a general protection function. The general principle of human dignity should be a potential source for new restrictions on the freedom of contract under European law. The positions of the market failure thesis affect the regulation of information duties applicable upon entry into financial services contracts. Such a regulation is not so much connected with consumer protection as conditioned by the specific nature of the financial market and can be justified by the special role banking plays in society. Security of society is a condition prerequisite to the continuation of mankind and outweighs other values. Because of the dangers posed by the crimes of money laundering and terrorism, prevention of such crimes can be treated as serving prevailing public interest, which sufficiently justifies the public authorities' imposing obligations on credit and financial institutions, including restricting the freedom of contract. It is sufficient grounds to require customers to provide during pre-contractual negotiations information about themselves to the extent provided for by law. The need to ensure security and the sustainability of society extends the protection obligation in contractual relations to those who are not party to the contract.

⁵⁸ Violation of the requirements of identification and verification and failure to apply international sanctions is punishable under the penal law. See MLTFPA §§ 57 and 63, and §§ 931 and 395 of the Penal Code (Karistusseadustik. – RT I 2001, 61, 364; 2008, 33, 200; in Estonian).



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The Draft Common Frame of Reference's Regulation of Unjustified Enrichment: Some Observations from Estonia's viewpoint

1. Introduction

Questions regarding the harmonisation of private law have evoked several debates in the European Union in the last few decades. These have expanded and become livelier especially in connection with the European Civil Code project.^{*1} The process of harmonisation of European private law also affects Estonia, even in areas not regulated by European Union legislation mandatory for the Member States. Thus, for example, the Principles of European Contract Law^{*2} (PECL) and the UNIDROIT Principles of International Commercial Contracts^{*3} (PICC) played a special role in the drafting of the Estonian Law of Obligations Act^{*4} (LOA).

On 28 December 2007, the European Commission was presented with the Draft Common Frame of Reference^{*5} (DCFR), which comprises the principles, definitions, and model rules of European private law. As the general provisions of the law of obligations in the Draft Common Frame of Reference are based on the PECL^{*6}, it is likely that the need to supplement or amend existing Estonian legislation in light of the general principles set out in the DCFR may more particularly concern the specific provisions of the Law of Obligations Act, among them the provisions pertaining to non-contractual obligations^{*7}, including unjustified enrichment law. With regard to the DCFR, the following functions are given primary emphasis: 1) a model for a political Common

¹ Available at <http://www.sgecc.net/pages/en/introduction/index.introduction.htm> (20.08.2008).

² The Principles of European Contract Law. Parts I (1995, 1999) and II (1999). O. Lando, H. Beale (eds.). The Hague 2000; part III (2003). O. Lando, E. Clive, A. Prüm, R. Zimmermann (eds.). The Hague 2003.

³ Principles of International Commercial Contracts. Rome: UNIDROIT 1994.

⁴ Võlaõigusseadus. – RT I 2001, 81, 487; 2005, 61, 473 (in Estonian); available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (20.08.2008).

⁵ C. von Bar, E. Clive, H. Schulte-Nölke (eds.). Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference. Interim Outline Edition. München: Sellier 2008. Available at <http://www.law-net.eu/> (21.08.2008).

⁶ DCFR (Note 5), pp. 2–27.

⁷ P. Varul. The Creation of New Estonian Private Law. – European Review of Private Law 2008 (16) 1, pp. 95–109.

Frame of Reference, envisaged by the European Commission in its Communication document of 2003⁸; 2) an academic text as a model for teaching and research work, aiding in understanding of the similarities of the private law in the jurisdiction of the European union; and 3) a source of inspiration for the legislators of countries in the process of modernising national law.⁹

This article examines the third of the above-mentioned functions and discusses the regulation of unjustified enrichment within the DCFR in comparison with the existing Estonian legislation. The objective of this article is to answer the question of whether and to what extent the DCFR could serve as an inspiration for the amendment, supplementation, or interpretation of Estonian unjustified enrichment law. On account of limitations of space, the article focuses on only some aspects of DCFR unjustified enrichment model rules, among them the prerequisites for claims for the transfer of that which is received without legal basis, the method for reversing enrichment, and the calculation of compensation, and it compares the solutions provided to those of existing Estonian legislation. The article also discusses certain questions regarding delimitation of the rules of unjustified enrichment and *negotiorum gestio*.

2. Unjustified enrichment regulation within the Common Frame of Reference and the Estonian Law of Obligations Act

Unjustified enrichment law is a traditional part of the law of obligations in the legal systems of Continental Europe¹⁰, regulating situations in which one person has received something (i.e., been enriched) to the disadvantage of another person without legal basis. As European directives have almost no regulation on questions related to unjustified enrichment law¹¹, the DCFR comprises the first attempt to outline the common principles of unjustified enrichment law in the Member States. The Study Group on a European Civil Code adopted the common principles for unjustified enrichment in Tartu in late 2005, and these are included in Book VII of the DCFR.

2.1. Delimiting the unjustified enrichment law from the provisions regarding *negotiorum gestio*

2.1.1. The regulation and prerequisites for application of *negotiorum gestio*

As part of its earlier work, the Study Group on a European Civil Code has developed the common European principles of *negotiorum gestio*¹², which, similarly to unjustified enrichment law, must fill the gaps that might appear between the rules of violation law and contract law. Regulation of benevolent intervention is included in Book V of the DCFR and applies where a person (the intervener) acts predominantly with the intention of benefiting another (the principal) while lacking the principal's prior consent.¹³

In Estonia, benevolent intervention in another's affairs is governed by Chapter 51 of the Law of Obligations Act which entered into force on 1 July 2002. Before the enactment of the Law of Obligations Act, situations involving benevolent intervention were subject to § 477 of the Estonian SSR Civil Code¹⁴ (CC), laying down

⁸ Communication from the Commission to the European Parliament and the Council: A more coherent European Contract Law. An Action Plan. COM(2003) 68 final, 12 February 2003.

⁹ DCFR (Note 5), pp. 6–8.

¹⁰ R. Zimmermann. Grundstrukturen des Europäischen Bereicherungsrechts. Mohr Siebeck 2005, p. 21.

¹¹ As an exception, Directive 97/7/EC lays down the principle that in the case of inertia selling to the consumer, a sender engaged in economic and professional activities has no claims against the consumer. See Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts. – OJ L 144, 4.06.1997, pp. 0019–0027.

¹² C. von Bar. Principles of European Law, Benevolent Intervention in Another's Affairs. Sellier 2006.

¹³ Article V.–1:101: Intervention to benefit another

(1) This Book applies where a person (the intervener) acts with the predominant intention of benefiting another (the principal) and:

(a) the intervener has a reasonable ground for acting; or

(b) the principal approves the act without such undue delay as would adversely affect the intervener.

(2) The intervener does not have a reasonable ground for acting if the intervener:

(a) has a reasonable opportunity to discover the principal's wishes but does not do so; or

(b) knows or can reasonably be expected to know that the intervention is against the principal's wishes.

¹⁴ Eesti NSV tsiviilkoodeks. – ENSV ÜVT 1964, 25; RT I 2001, 47, 260 (in Estonian).

the obligation to return assets obtained or saved without legal basis. Thus, no separate *negotiorum gestio* law was recognised. This also means that, so far, Estonia has lacked significant amounts of judicial practice regarding the delimiting of unjustified enrichment and *negotiorum gestio*, and the application of the rules pertaining to *negotiorum gestio* depends upon the date of the activity constituting the object of dispute. Namely, according to § 21 of the Law of Obligations Act, General Part of the Civil Code Act and Private International Law Act Implementation Act^{*15}, the provisions of the Law of Obligations Act related to *negotiorum gestio* apply to acts performed after 1 July 2002; § 23 foresees that the provisions of the Law of Obligations Act concerning unjustified enrichment apply in cases of unjustified enrichment occurring after 1 July 2002. Hence, if a person paid costs for the benefit of another prior to the enactment of the Law of Obligations Act and continued to do so after the enactment thereof, a situation could have arisen in which some of the costs must be compensated for pursuant to § 477 of the CC and some of them under the provisions of the LOA (and the application of the Law of Obligations calls for determining whether the situation constituted *negotiorum gestio* or unjustified enrichment).

According to § 1018 of the Law of Obligations Act, *negotiorum gestio* is deemed to be justified if a person (the *negotiorum gestor*) acts for the benefit of another person (the principal) without being granted the right or being obliged by the principal to perform the act and the *negotiorum gestor* has justification for the act, meaning that 1) the principal approves of the act; 2) the act corresponds to the interests and actual or presumed intention of the principal; or 3) in the case of failure to act, the principal's obligation arising from the law to maintain a third party would not be performed in a timely manner or the act is essential in view of the public interest for another reason. If, in the absence of such justification, the *negotiorum gestor* acted for the benefit of another person with the intention of benefiting said person, this constitutes unjustified *negotiorum gestio*.

Both in the common European principles and in Estonian law, the rules of *negotiorum gestio* have priority over unjustified enrichment regulation: *negotiorum gestio* can constitute the legal basis on account of which a person may have received any thing from another.^{*16}

The problems related to the delimiting of unjustified enrichment and *negotiorum gestio* could be characterised on the basis of the following example^{*17}:

In 1999, cohabitants A and B commenced the construction of an annex to the dwelling of B's aunt C with her knowledge and consent, with the purpose of settling in the annex. When B died in 2003, A continued paying expenses related to the annex. In 2004, C denied A access to the annex. A filed a claim against C for compensation of the expenses he incurred and that B had paid (insofar as A is heir to B) for building the annex. In court, it was not established that A and B had ever concluded a contract with C regarding the construction of the annex.

With application of the provisions of the DCFR, pursuant to Articles V.-1:101 and V.-3:101, A would be entitled to compensation for reasonable costs incurred for the purpose of the action, if he and B acted with the predominant intention of benefiting C and they had reasonable grounds for their action, or C approved of the act without such undue delay as would adversely affect the interveners. The first question would thus be whether this case constituted *negotiorum gestio* or whether unjustified enrichment is to be held applicable. For A and B, the purpose of constructing the annex was to ensure a future dwelling. Is this to be deemed acting predominantly in their own interest or predominantly in C's interest (as the activity constituted improving her property)? In the eyes of the judge, this criterion may be too ambivalent.^{*18} If one were to deem A and B to have acted with the predominant intention of benefiting C, the further choice between *negotiorum gestio* and unjustified enrichment law depends on whether the action was reasonable (in this case it probably was, as commencement of the work occurred with the knowledge and consent of C).

Pursuant to Estonian legislation, the proportion of the interest of the parties to an obligation is not a significant factor; even a half wish to do something for the benefit of another is sufficient.^{*19} Thus, *negotiorum gestio* law could be applied here: A and B have done something for the benefit of C, and the action complied with C's interests and actual or presumed intention.^{*20}

¹⁵ Võlaõigusseaduse, tsiviilseadustiku üldosa seaduse ja rahvusvahelise eraõiguse seaduse rakendamise seadus. – RT I 2002, 53, 336; 2005, 39, 308 (in Estonian); available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (20.08.2008).

¹⁶ C. von Bar (Note 12), p. 72; T. Tampus. Lepinguväliste võlasuhete õigus (Non-contractual Obligations Law). Tallinn: Juura 2007, p. 66 (in Estonian); CCSCd 5.12.2007, 3-2-1-107-07, p. 18. – RT III 2007, 45, 362 (in Estonian); CCSCd 16.06.2008, 3-2-1-54-08, p. 13. – RT III 2008, 30, 205 (in Estonian).

¹⁷ Pursuant to CCSCd 3-2-1-107-07, 5 December 2007. – RT III 2007, 45, 362 (in Estonian).

¹⁸ H. Sprau. Benevolent Intervention in Another's Affairs: Some remarks on the Draft Report Presented by the Study Group on a European Civil Code. – ERA-Forum 2/2006, p. 224.

¹⁹ T. Tampus (Note 16), p. 45.

²⁰ In this case, referring the case to a lower court for a new hearing, the Supreme Court still mentioned that the court has yet to determine, whether the case constitutes *negotiorum gestio* within the meaning of § 1018 of the Law of Obligations Act; if not, unjustified enrichment law is to be applied (paragraph 17 of the court judgment).

2.1.2. Obligation to transfer pursuant to *negotiorum gestio* and unjustified enrichment law

Pursuant to both the DCFR and the Law of Obligations Act, the *negotiorum gestor* has the obligation to transfer that which is received as a result of his or her acts to the principal^{*21} and has the right to demand compensation for costs that he or she incurs or be released from obligations that he or she has assumed.^{*22} In the above example, A can thus demand that C compensate for the costs incurred in construction (e.g., costs for buying construction materials), on the presumption that A and B did not intend to demand that the principal compensate for costs when beginning to act (see § 1023 (3) of the Law of Obligations Act) or at the time of acting (see DCFR, Art. V.–3:104).^{*23} If A also wants to demand a reward for construction work that he and B performed, he must bear in mind that only a person acting in the course of his or her economic or professional activities has the right to demand a reward for the work performed.^{*24}

Where the action of the intervener is unreasonable and not approved by the principal, Book V of the DCFR does not apply. In such a case, the rights and obligations of the parties must primarily be subjected to unjustified enrichment law. The same applies in cases where the intervener was acting on behalf of another in his or her own interests.^{*25}

Section 1024 (4) of the Law of Obligations Act provides that in the case of unjustified *negotiorum gestio*, the principal shall transfer that which is received as a result of the action to the *negotiorum gestor* pursuant to the provisions concerning unjustified enrichment if the *negotiorum gestor* was *bona fide* (i.e., at the time the *negotiorum gestor* begins to act, that person does not understand and is not required to understand that he or she lacks justification for acting). Thus, if C's obligation of transfer were to be subject to unjustified enrichment law (§ 1042) on the basis of the above example, A would be in a somewhat more favourable position, as neither the DCFR nor the LOA allows avoidance of A's claim for compensation on the grounds that when beginning to construct or at the time of constructing the addition A and B did not intend to demand compensation for costs. A could also file a claim for a reward for the work performed on the grounds that C has, among other things, been enriched by dint of avoiding costs to commission the work. It must nevertheless be considered that also the application of unjustified enrichment law may preclude A's claim for compensation of costs^{*26}, for instance, if it appeared that A and B had failed, on account of circumstances arising from their action, to notify C in time of the intent to incur costs; if C had contested the incurring of the costs in advance; or if building an annex to the dwelling in question had not been in accordance with the law.

It is thus important to note that pursuant to both the DCFR and the Law of Obligations the *post-factum* approval of the principal makes unjustified *negotiorum gestio* justified — this means that instead of unjustified enrichment law, *negotiorum gestio* will apply, enabling preclusion of the intervener's demand for reward and in some cases the claim for the compensation of costs altogether.

²¹ DCFR V.–2:103 (1) and Law of Obligations Act § 1021.

²² DCFR V.–3:101 and Law of Obligations Act § 1023.

²³ In the litigation underlying the abovementioned example, the court of appeal considered it necessary to mention that “...in a situation where (B) spent all of their resources for creating a home for their family, and this purpose was not realised due to the intention of the defendant, it cannot be presumed that in the case of not reaching a compromise, costs will not be demanded.

²⁴ DCFR V.–3:102 and Law of Obligations Act § 1023 (2).

²⁵ C. von Bar (Note 12), p. 102.

²⁶ LOA § 1042. Requirement to compensate costs

1) A person who incurs costs with regard to an object of another person without a legal basis therefor may demand compensation of the costs to the extent to which the person on whose object the costs are incurred has been enriched thereby, taking into consideration, *inter alia*, the fact of whether such costs are useful to the person and the intent of the person with regard to the object. Determination of the extent of enrichment shall be based on the time when the person with regard to whose object costs are incurred has the object returned or is able to begin to use the increased value of the object in any other manner.

(2) A person who incurs costs has no right of claim provided for in subsection (1) of this section if:

1) the person with regard to whose object costs are incurred demands the removal of improvements made by means of the incurred costs and if the removal of such improvements is possible without causing damage to the improvements;

2) the person who incurs costs fails, due to circumstances arising from the person, to notify the other person in time of the intent to incur costs;

3) the person with regard to whose object costs are incurred has contested the incurring of the costs in advance; the incurring of costs with regard to the object is prohibited arising from law or the contract.

2.1.3. Expiry of claims

In the application of Estonian law, the regulation of the expiry of claims pursuant to the General Part of the Civil Code Act (GPCCA)²⁷ is also somewhat different: the claims constitute claims arising from law, where according to the general rule in the case of *negotiorum gestio* the limitation period for a claim for compensatory costs shall be 10 years from the moment when the claim falls due (GPCCA, § 149); in the case of a claim arising from unjust enrichment, however, § 151 foresees a double expiry: the limitation period for a claim arising from unjust enrichment shall be three years from the moment at which the entitled person became or should have become aware of the claim arising from unjust enrichment. In any case, however, a claim arising from cause of unjust enrichment expires no later than 10 years after the unjust enrichment occurred. Hence, if C fails to approve the incurring of costs, A has the right of claim for compensation of costs against C pursuant to § 1042 of the Law of Obligations Act, which A is to file within three years from the time of becoming aware of the claim as such. If C approves of incurring costs, the limitation period for a claim for compensation of costs incurred in *negotiorum gestio* shall be 10 years from the moment when the claim falls due.

2.2. Classification of claims arising from unjustified enrichment

2.2.1. Different classification options

In the laws of those European countries that regulate unjustified enrichment as a separate area of the law²⁸, considerable differences occasionally can be seen in the classification of claims. Some legal systems, for instance, differentiate between the performance of an undue obligation (derived from the claim of *conditio indebiti* known in Roman law: the payment of a non-existing debt or the repayment of a debt already paid) and unjustified enrichment (comprising other situations wherein a person had no legal basis for enriching another).²⁹ Claims arising from unjustified enrichment can be classified according to whether enrichment has occurred on the basis of performance or by another method.³⁰ Thirdly, it can be noted that, while Continental European law concentrates on identifying the absence of legal basis, a Common Law lawyer instead seeks justification explaining why the enrichment is unjustified.

Proceeding from the differences listed, there are plenty of people who doubt the possibility of harmonisation of unjustified enrichment law³¹, but the existence of differences paradoxically also serves as the argument used to justify the necessity of harmonised principles.³² E. McKendrick has named several reasons supporting the importance of classifying claims: this ensures similar resolution of similar cases, brings out the inconsistencies in existing rules, contributes to greater clarity and understanding of the entire set of rules, and also has economic importance: the solution is easier to find if the structure of the law is clear.³³

The multitude of existing solutions forces the harmoniser of unjustified enrichment principles to either choose one of the existing classifications or introduce a new one. There are supporters of a typologised catalogue of claims (classification of claims on the basis of whether enrichment occurred through performance or another method)³⁴ and also are spokesmen for a unitary approach (a comprehensive general rule followed by more specific provisions)³⁵ — with both resting their case on simplicity and intelligibility.

²⁷ Tsiviilseadustiku üldosa seadus. – RT I 2002, 35, 216; 2007, 24, 128 (in Estonian). Available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (20.08.2008).

²⁸ In this aspect the Nordic Countries (where the answer to this question is negative) differ from other Member States. See in further detail: P. Schlechtriem. *Restitution und Bereicherungsausgleich in Europa I*. Tübingen: Mohr Siebeck 2000, p. 49 ff.

²⁹ E.g., in French, Dutch, Spanish and Italian law.

³⁰ E.g., German law; a modernised version of such a division is also followed in Chapter 52 of the Estonian Law of Obligations Act.

³¹ W. J. Swadling. *Restitution and Unjust Enrichment*. – A. Hartkamp *et al.* (ed.). *Towards a European Civil Code*. Martinus Nijhoff Publishers 1994, p. 282; the same also E. McKendrick: E. McKendrick. *Taxonomy: Does it Matter?* – D. Johnston, R. Zimmermann, D. Johnston, R. Zimmermann (ed.). *Unjustified Enrichment: Key Issues in Comparative Perspective*. Cambridge University Press 2002, p. 656; also J. Smits. *A European Law of Unjustified Enrichment? A Critical View of the Law of Restitution in the Draft Common Frame of Reference*. – European Private Law Beyond the CFR, Antony Vaquer (ed.). Tilburg 2008. Available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1103826 (10.05.2008).

³² C. von Bar. *The Principles of European Law on Benevolent Intervention in Another's Affairs and on Unjustified Enrichment*. – ERA-Forum 2/2006, p. 213; similarity in substantive solutions is admitted also by other authors. Cf. P. Schlechtriem, C. Coen, R. Hornung. *Restitution and Unjust Enrichment in Europe*. – *European Review of Private Law* 2001/2–3, p. 415.

³³ E. McKendrick (Note 31), pp. 632–637.

³⁴ P. Schlechtriem. *Europäisierung des Bereicherungsrechts*. 2002, p. 20. Available at <http://www.ejcl.org/74/art74-3.PDF> (15.04.2008).

³⁵ E. Clive. *Unjustified Enrichment*. – A. Hartkamp *et al.* (ed.). *Towards a European Civil Code*. Kluwer Law International 2004, p. 587.

2.2.2. Classification of claims arising from unjustified enrichment within the DCFR

Book VII of the DCFR has decided in favour of the unitary model, introducing first the basic rule^{*36}, followed by qualifying provisions regarding the elements of unjustified enrichment, the content and extent of claims against enrichment, defences (disenrichment), and relations to other legal rules. There is thus no classification according to the types of enrichment. This has been justified with the wish to follow the structure applied with regard to the principles of violation law assembled in Book IV, and for the purpose of avoiding excess, the text as a whole was kept relatively lean.^{*37} By leaving enrichment attributable to performance and the enrichment attributable to another's disadvantage undifferentiated, an attempt is made to avoid the situation where one and the same situation would be resolved differently in different legal systems on account of consensual variance regarding the definition of performance.^{*38} Additional prerequisites to the basic rule are laid down in the following rules, which are to be interpreted by the party that is the applicant.

The classification of DCFR claims has already occasioned certain criticism from the above-mentioned economic standpoint: it has been found to constitute not principles but very abstract technical regulations with a structure and logic not readily understood by national judges or lawyers.^{*39}

2.2.3. Classification of claims arising from unjustified enrichment within the Law of Obligations Act

In Estonia, obligations arising from unjustified enrichment are governed by the Law of Obligations Act of 1 July 2002, which is significantly more thorough than the provisions of the Estonian SSR Civil Code, formerly in force^{*40}; all told, Chapter 52 of the Law of Obligations Act comprises 16 sections in four divisions. A recognisable model for systematising the provisions of Chapter 52 of the Law of Obligations Act is the scheme applied for reforming unjustified enrichment law in the German Civil Code, which was never applied in practice in Germany.^{*41}

Division 1 of Chapter 52 includes a general provision (§ 1027) laying down the rule that a person shall transfer to another person, on the bases of and to the extent provided for in that chapter, that which is received from that another person without legal basis. The claims contained in the following sections can be classified according to whether enrichment has occurred by way of performance (performance condition — Division 2) or not (non-performance condition — Divisions 3 and 4).

Division 2 of Chapter 52 governs reclamation of that which is received as a result of performance of obligations, divided into the general composition (§ 1028) and specific cases: reclamation of what is transferred to a third party at the order of the obligee or person believed to be an obligee (§ 1029), reclamation of that which is transferred to a third party for performance of a contract entered into for the benefit of the third party (§ 1030), and reclamation of that which is transferred to a new obligee in the case of waiver of claims (§ 1031).

The sections in Division 3 discuss compensation in the event of violation of rights (violation condition, § 1037) and the specific cases thereof — disposal of an object by a person not so entitled (§ 1037 (2)), disposal without charge by an unentitled person (§ 1040), and performance of an obligation in favour of a person not entitled to accept performance (§ 1037 (4)).

Division 4 governs compensation for costs (performance of an obligation of another person, in § 1041, or incurring of costs with respect to an object of another person, in § 1042) incurred for the benefit of other persons.

It has been noted that the structure of Chapter 52 of the Estonian Law of Obligations Act is in compliance with the main elements of the European unjustified enrichment law and is very progressive.^{*42} If one were to add that, as mentioned above, several authors find that the differences regarding the classification of claims and terminology do not prevent reaching substantively similar resolutions in unjustified enrichment cases in different legal systems^{*43}, it may be deduced that the Estonian legislator has no need to take the DCFR as a model for restructuring the rules related to unjustified enrichment.

³⁶ DCFR VII.-1:101: Basic rule. (1) A person who obtains an unjustified enrichment which is attributable to another's disadvantage is obliged to that other to reverse the enrichment.

³⁷ C. von Bar (Note 32), pp. 216–217.

³⁸ S. Swann. A Guide to the Principles of European Law on Unjustified Enrichment. – ERA-Forum 2/2006, p. 236.

³⁹ C. Wendehorst. The draft principles of European unjustified enrichment law prepared by the study group on a European civil code: A comment. – ERA-Forum 2006/2, p. 259.

⁴⁰ Section 477 of the Civil Code laid down the obligation of returning assets obtained or saved without legal basis, and § 478 listed assets not subject to returning.

⁴¹ R. Zimmermann. Unjustified Enrichment: The Modern Civilian Approach. – Oxford Journal of Legal Studies 1995 (15) 3, pp. 425–429.

⁴² P. Schlechtriem. The New Law of Obligations in Estonia and the Developments Towards Unification and Harmonisation of Law in Europe. – Juridica International 2001 (VI), p. 21.

⁴³ See Note 32.

2.3. Prerequisites for a claim arising from unjustified enrichment in the DCFR as compared with the provisions of the Law of Obligations Act

The tests for an unjustified enrichment claim comprise four elements pursuant to the DCFR: when enrichment is unjustified, enrichment, disadvantage, and enrichment that is attributable to disadvantage of another (chapters 2, 3, and 4 of Book VII). Pursuant to Estonian law, the specific prerequisites for every single claim are dependent upon what claim (condition) it constitutes, or on the way in which someone has been enriched on account of another.

2.3.1. When enrichment is unjustified

In the first test — concerning when enrichment is unjustified — it is presumed that enrichment of a person to the disadvantage of another person is unjustified unless the enriched person was entitled to the enrichment by virtue of a contract or other juridical act, a court order, or a rule of law (see VII.–2:101 (a)) or unless the disadvantaged person consented freely and without error to the disadvantage (VII.–2:101 (b)). Therefore, if D has transferred money to E's account pursuant to a valid contract, the circumstance does not constitute unjustified enrichment, even if D performed the transfer by mistake, having no intention to transfer the money to E but instead wishing to set off E's claim with her own claim against E. The DCFR does not foresee the application of unjustified enrichment provisions even when D performed a money transfer to E's account knowingly and without error, without being under obligation to do so by virtue of a contract, rule of law, or court order.

In the Law of Obligations Act, enrichment is deemed to be unjustified if it has occurred without legal basis (in § 1027); what exactly is deemed to be this legal basis precluding the application of unjustified enrichment law proceeds from judicial practice — for instance, a valid contract^{*44}, *negotiorum gestio*^{*45}, a court judgement^{*46}, or legislation.^{*47}

In the case of **performance condition**, the Law of Obligations Act does not lay down a single rule providing that enriching another person without legal basis freely and without error would preclude the claim against unjustified enrichment.^{*48} In the theoretical discourse, the common view is that a person knowingly enriching another person without legal basis should not have the right of recourse pursuant to the principle of good faith.^{*49} Here it could be asked whether the transferor's knowledge about the absence of legal basis could not be laid down in Estonian legislation *expressis verbis* as the basis for refusal of returning that which has been transferred, as provided in the DCFR. One supporting argument could be that, according to the *negotiorum gestio* regulation of the Law of Obligations Act, the claim against unjustified enrichment is precluded in the case of unjustified *negotiorum gestio* in bad faith — i.e., if the *negotiorum gestor* was or had to be aware that he or she lacked justification for acting on behalf of another (LOA, § 1024 (4)) and the principal does not approve of the action. An answer to this question could be sought through the following example:

Buyer A enters into an unattested written preliminary contract with seller B to purchase a flat in Tallinn and pays the agreed advance payment. Pursuant to the law, the preliminary transfer contract for an immovable must be concluded in a notarially attested form, and thus the contract concluded between A and B is void because of failure to adhere to a formal requirement.

This constitutes a performance condition: person A has completed a performance^{*50} with respect to B without legal basis, as the contract is void. If the law precluded A's claim for compensation in the case that A was aware of the contract being void, it may be asked how this can be adequately determined and how the burden of proof has been apportioned. This might entail a situation wherein A's claim may depend upon A's person: can A demand a refund of the advance payment if A is a citizen of a foreign country who does not speak Estonian and is unaware of Estonian legislation? If A, however, constantly does business in Estonia and uses the services of an Estonian advocate's law office, is the claim then precluded? What about the case in which A is an Estonian citizen but lacks juridical special knowledge? Would A have a claim if lacking the juridical

⁴⁴ CCSCd 3-2-1-46-07, 16 May 2007. – RT III 2007, 21, 176 (in Estonian).

⁴⁵ CCSCd 3-2-1-91-06, 1 November 2006. – RT III 2006, 40, 343 (in Estonian); CCSCd 3-2-1-107-07 (Note 16) and 3-2-1-54-08 (Note 16).

⁴⁶ CCSCd 3-2-1-25-06, 9 September 2006. – RT III 2006, 24, 221 (in Estonian); CCSCd 3-2-1-107-04, 19 October 2004. – RT III 2004, 27, 296 (in Estonian).

⁴⁷ ACSCd 3-3-1-56-04, 30 November 2004. – RT III 2004, 35, 363 (in Estonian).

⁴⁸ It has, however, been laid down that the recipient who was or had to be aware of circumstances constituting unjustified transfer, can not rely on no basis for enrichment (LOA § 1035 (1)).

⁴⁹ T. Tampuu (Note 16), p. 75.

⁵⁰ A performance is understood as the knowing and purposeful increasing of foreign assets. See P. Schlechtriem. *Võlaõigus. Eriosa* (Law of Obligation. Specific part). Tallinn: Juura 2000, p. 214 (in Estonian).

knowledge in circumstances where the newspapers had written a lot about the fact that the preliminary contract for purchasing an immovable asset must be in a notarially attested form?

The aim of this line of thought is to demonstrate that the transferor's awareness of the absence of legal basis can in practice be difficult to prove if more objective criteria have not been laid down.

Applying the provisions of the DCFR, the buyer could still demand a refund of the advance payment paid pursuant to a void contract, as the DCFR deems enrichment to be unjustified also in the case where it occurs for a purpose which is not achieved or with an expectation which is not realised, if the enriched person knew of, or could reasonably be expected to know of, the purpose or expectation and if the enriched person accepted or could reasonably be assumed to have accepted that the enrichment must be reversed in such circumstances.^{*51} As A made advance payment with the purpose of becoming the owner of the flat in the future, the purpose was not realised and B could reasonably be expected to agree to refund the advance payment.

The principle described here was laid down in the original text of the draft legislation of the Law of Obligations Act^{*52} but was deleted from the act as passed by the Riigikogu. Thus, laying down the transferor's awareness in the Law of Obligations Act as a prerequisite precluding claim against unjustified enrichment would not be justified without addition of a provision comparable to Article VII.-2:101 (4) of the DCFR, as otherwise this could lead to an unjust solution with respect to the transferor. In specific situations it would be more purposeful to rely on the principle of good faith, established in the general part of the Law of Obligations Act.^{*53}

In the event of a claim filed for redress of **violation of the right of another person**, the awareness of the person knowingly enriching another person concerning the lack of legal basis serves as a circumstance precluding the claim for compensation in Estonian legislation: § 1037 (1) LOA establishes that a person who violates the right of ownership, another right, or the possession of an entitled person by disposal, use, consumption, accession, confusion, or specification thereof without the consent of the entitled person or in any other manner (i.e., a violator) shall compensate the entitled person in the amount of the usual value of anything received through the violation.

In the event of **incurring costs for the benefit of other persons**, there is some reference to the awareness of the person enriching another person in § 1042 (2) 2) LOA: the claim for compensation of costs incurred with regard to an object of another person depends on whether the person incurring costs has notified the other person in time of the intent to incur costs, and if not, whether the failure to notify was due to circumstances arising from the person incurring costs (see LOA, § 1042 (2) 2)). It thus follows that a person who was aware of not having a legal basis for enriching the other person and who failed to report his or her intent may remain without the right to claim compensation.

Example: O buys a used car and has it repaired. It later emerges that the car had been stolen from P. Accordingly, P demands the car back, and O can demand the compensation of costs pursuant to § 1042. His claim is precluded if, prior to having the car repaired, he learned that the car had been stolen and, in consequence of circumstances arising from himself, failed to notify the actual owner of the car.

If incurring costs for the benefit of another consists of performing an obligation of that person, the performer's awareness of the absence of legal basis means a wish to benefit the other person, and therefore one first must assess whether this constitutes *negotiorum gestio* and whether the action is justified or unjustified.

Example: D believes that her child broke the spectacles of E's child in school and compensates E for the amount necessary to buy new glasses. It then becomes clear that it was F's child who broke the glasses.

As in the latter example D had no intent to benefit F, this does not constitute *negotiorum gestio*.^{*54} D has a claim for compensation against F pursuant to unjustified enrichment rules, because F has been released from the obligation to compensate E for the cost of the glasses.

⁵¹ DCFR VII.-2:101 (4). At the same time, the DCFR does not foresee a limitation for the right of recourse of that which is transferred in case the expected purpose was not realised due to circumstances arising from the transferor themselves.

⁵² Draft LOA § 1136 (1) laid down that upon transferring something not for performing an obligation but for the purpose of causing the recipient to act in a certain way, that which is received can be demanded to be returned in the event of non-occurrence of the intended behaviour, if the recipient understood or ought to have understood the transferor's such intention. Section 1132 (2) 2) of the draft laid down that the right to demand the return of that which is received does not exist if the recipient could reasonably presume that the person wanted the recipient to keep that which is received regardless of absence of legal basis for the abovementioned circumstances. See draft Law of Obligations Act (116 SE I), <http://web.riigikogu.ee/ems/saros-bin/mgetdoc?itemid=991610001&login=proov&password=&system=ems&server=ragne11> (10.08.2008) (in Estonian).

⁵³ LOA § 6. Principle of good faith: (1) Obligees and obligors shall act in good faith in their relations with one another. (2) Nothing arising from law, a usage or a transaction shall be applied to an obligation if it is contrary to the principle of good faith.

⁵⁴ LOA § 1018 (2): A case where a person has no desire to act for the benefit of another person is not deemed to be *negotiorum gestio*.

2.3.2. Enrichment and disadvantage

The second prerequisite, enrichment, has been defined more precisely in the DCFR than in the Law of Obligations Act: it consists of increase in assets or a decrease in liabilities of a person, receiving a service or having work done, or use of another's assets (Art. VII.–3:101 (1)). According to the drafters of the DCFR, they knowingly left the concept of assets undefined; this may, in addition to physical things, also comprise rights, including personality rights, as well as legal positions of commercial value.^{*55}

The third prerequisite is disadvantage, constituting an opposite situation to enrichment, a so-called reflection. This constitutes a new term introduced by the study group^{*56}, which shall be discussed alongside enrichment.

The concept of enrichment within the ambit of the Common Frame of Reference does not so much denote the comparison of the difference or net value of the financial situation of the parties to the obligation as it concentrates on the movement of objects^{*57} — thus simplifying the filing of claims on the basis of mutual annulled contracts, if the annulment occurs after performance of mutual obligations. Evaluating only the economic effect would mean that receipt of an object that is worthless or demands large expenses could not be deemed to be enrichment; neither would it constitute enrichment in that case when a service has been performed for a person who has not requested it.^{*58}

In Estonian legal literature, enrichment is defined as obtaining monetary benefit, which may consist of receiving something, being relieved of something, or saving something, whether through an unjustified performance, via unjustified intervention into rights, or by other means.^{*59} The Law of Obligations Act has not defined the concept of enrichment (or of disadvantage). It employs the expression 'that which is received', which can be interpreted similarly to the language of the DCFR: this could be property or possession, legal status arising from an entry in the land register^{*60}, a claim or other right^{*61}, avoidance of costs^{*62}, release from obligations, etc.

The pointing out of **service as a form of enrichment** in the DCFR deserves separate comment. Pursuant to Article VII.–3:101 (1) (b), unjustified enrichment also occurs in a situation where a person has received a service without legal basis, both in the case of the parties not having entered into a contract for provision of services and in the case of having entered into a contract that is void.^{*63}

As is mentioned above, the Law of Obligations Act does not define 'that which is received' and therefore does not include direct reference to receiving a service as a separate form of enrichment. According to the provisions applying to contracts for provision of services (LOA, Part 8), 'service' can refer to performing a mandate as well as performing work (manufacture or alteration of a thing or obtaining of a different result).

A situation in which a person has provided a service for another but the parties have never entered into a contract can be deemed to be *negotiorum gestio* or unjustified enrichment, depending on whether the provider of the service has the intent to benefit the other person.

The situation would be less clear if the parties had entered into a contract but the contract is void. In its § 1042, the Law of Obligations Act lays down valid claims for compensation for costs incurred with relation to an object of another person and could therefore, logically, also refer to applicability in the event of void contracts for provision of services. At the same time, the structure of Chapter 52 of the Law of Obligations Act must be kept in mind here: performance of a void contract constitutes a performance, governed by Division 2 of said chapter, and thus § 1042 is not applicable. Arguments can be found in Estonian legal discourse in favour of provisions addressing *negotiorum gestio*: application of the provisions on *negotiorum gestio* would yield a fairer result with regard to claims for compensation of costs, as the law on *negotiorum gestio* contains several specific provisions addressing non-contractual liability for damage, which protect the interests of a person justifiably acting for the benefit of another person and foresee the increased liability of a *negotiorum gestor* acting in bad faith. In addition, the application of *negotiorum gestio* provides better protection for the principal, as in the event of unjustified *negotiorum gestio* performed in bad faith the *negotiorum gestor* does not have a claim for compensation.^{*64}

⁵⁵ S. Swann (Note 38), p. 242.

⁵⁶ This term was thus the most difficult to translate when translating the DCFR unjustified enrichment provisions into Estonian, as there is no such concept in Estonian legal terminology.

⁵⁷ S. Swann (Note 38), p. 241.

⁵⁸ E. Clive (Note 35), p. 590.

⁵⁹ T. Tampus (Note 16), p. 59.

⁶⁰ CCSCd 3-2-1-129-05, 1 December 2005. – RT III 2005, 43, 426 (in Estonian)..

⁶¹ E.g., a privatisation voucher (CCSCd 3-2-1-119-06, 28 November 2006. – RT III 2006, 45, 378; in Estonian).

⁶² CCSCd 3-2-1-33-07, 2 May 2007. – RT III 2007, 20, 163 (in Estonian); CCSCd 3-2-1-107-07 (Note 16).

⁶³ In the case of void contracts on the provision of services the application of *negotiorum gestio* is precluded. See C. von Bar (Note 12), p. 110.

⁶⁴ T. Tampus (Note 16), pp. 42–43 and p. 67.

On the other hand, the following example could serve as a reminder of a nuance in differentiation between *negotiorum gestio* and unjustified enrichment — the question of reward:

K does not know that his neighbour, elderly lady L, is of restricted active legal capacity and has been assigned a guardian by the courts. L turns to K, asking him to remove the large trees on her lot and promising to pay her 3000 Estonian kroons for doing so. Nothing in L's behaviour refers to her mental condition. The trees are healthy and viable, and there is thus no actual need for cutting them down; L justifies the request with the wish to allow more sunshine on her lot.

In application of the law on unjustified enrichment, K has the opportunity to demand a reward for the work performed, even if cutting down trees does not constitute K's economic or professional activity. If one were to apply the *negotiorum gestio* law, it is, correspondingly, relevant whether K's activity is approved by L's guardian. In the absence of approval, pursuant to § 1024 (4), that which is received shall be transferred pursuant to the provisions concerning unjustified enrichment, so the outcome would be the same. If, however, L's guardian approves of K's activity, the latter can be deemed to be justified *negotiorum gestio* and K has the right to demand compensation for costs; it is not, however, possible to file a claim for reward, even though these terms had been agreed upon.

Had K known or had to have known about L's restricted active legal capacity, there would not be the obligation to transfer that which is received from L upon application of the law on *negotiorum gestio*. Unjustified enrichment regulation, as already mentioned, does not expressly preclude K's claim in the case of K acting in bad faith, but this gap could be filled here with the application of the principle of good faith.

That the above-mentioned problems are nothing unique to Estonian law is also supported by the fact that the question regarding legislation applicable to void contracts for provision of services has also been discussed in the approaches of German jurists and German judicial practice.⁶⁵ The subject is, however, relatively new in Estonia — after all, before 1 July 2002 there was no need to distinguish between *negotiorum gestio* and unjustified enrichment.

This leads to the viewpoint that, in determination of the applicable legislation in the event of services being provided on the basis of void contracts, the DCFR with its soon-to-be published comments could be most useful reference material for shaping Estonia's approach.

2.3.3. Attribution

The fourth prerequisite is the attribution of a person's enrichment to another's disadvantage. Pursuant to the DCFR, enrichment is attributable to another's disadvantage in particular where an asset of that other is transferred to the enriched person by that other, a service is rendered to or work is done for the enriched person by that other, the enriched person uses that other's asset, especially where the enriched person infringes the disadvantaged person's rights or legally protected interests, an asset of the enriched person is improved by that other, or the enriched person is discharged from a liability by that other (Art. VII.–4:101). An enrichment may be attributable to another's disadvantage even though the enrichment and disadvantage are not of the same type or value (Art. VII.–4:107).

The list established in Article VII.–4:101 actually matches the types of claims distinguished under Estonian law (see section 2.2.3 of this paper). Attribution of enrichment on one hand and disadvantage on the other denotes a situation defined as 'enrichment on behalf of another' in the case of all claims against enrichment in Estonian law.⁶⁶ No such prerequisite is expressly provided in the Law of Obligations Act, but it can be seen to proceed from both Estonian legal theory⁶⁷ and judicial practice: The Supreme Court has, for instance, noted that "pursuant to the meaning of § 1037 (1) LOA, the violator must acquire assets to the disadvantage of the tortfeasor — i.e., receive assets that by law should have been received by the tortfeasor".⁶⁸

2.4. Reversal of enrichment

2.4.1. Transfer or compensation

Pursuant to Article VII.–5:101 (1) and (2) of the DCFR, enrichment must be reversed by transferring the asset to the disadvantaged person; if a transfer would cause the enriched person unreasonable effort or expense, he or she must pay monetary compensation instead of transferring the asset. One could ask whether it should be

⁶⁵ C. von Bar (Note 12), pp. 145–147.

⁶⁶ Such a definition was wished to be avoided, as it comprises disadvantage and attribution — the prerequisites that are attempted to be distinguished. See C. von Bar (Note 32), p. 218.

⁶⁷ T. Tappuu (Note 16), p. 59.

⁶⁸ CCSCd 3-2-1-46-07, 16 May 2007, p. 11. – RT III 2007, 21, 176 (in Estonian).

necessary to repeat in the unjustified enrichment regulations of the DCFR what has already been established in Article III.–3:302 (3) (a) and (b) of Book III, laying down that performance of non-monetary obligations cannot be enforced where performance would be unlawful, impossible, or unreasonably burdensome or expensive for the debtor.

Article VII.–5:101 (4) of the DCFR also establishes that, to the extent that the enriched person has obtained substitute in exchange, the substitute is the enrichment to be reversed if the enriched person is in good faith at the time of disposal or loss and the enriched person so chooses (point a) or if the enriched person is not in good faith at the time of disposal or loss, the disadvantaged person so chooses and the choice is not inequitable (point b). The wording of the article does not expressly specify what is meant by 'substitute' in the DCFR — different forms of compensation or also objects received upon entry into an exchange contract.

Similarly to the DCFR, the regulation of the Law of Obligations Act is primarily aimed at returning that which is received in kind; if this is impossible, the recipient shall compensate in the amount of the usual value thereof as of the time when the right to reclaim was created (§ 1032 (2)). In the concurrence of Chapter 52 and the general provisions of the Law of Obligations Act, compensation can be considered in the stead of transfer if performance of the obligation is unreasonably burdensome or expensive for the party so obliged (§ 108 (2) 2)). Pursuant to the second sentence of § 1032 (1) LOA, in the event of the destruction or consumption of, damage to, or seizure of the transferred object, the transfer of that which is acquired in compensation for said object may be demanded (what is meant is, for instance, compensation for damage and insurance indemnities), but if the recipient has substituted the object in exchange for another object, for instance, the transferor's claim shall not be extended thereto, in contrast to what is suggested in the DCFR. In case the recipient offers to substitute monetary compensation for the transfer of an object, this is deemed to be substitution (§ 89 LOA) and its acceptability depends upon whether the transferor agrees to it.

The solution offered by the regulations of the DCFR and the Law of Obligations Act can be compared with the following example:

A purchases a tractor from B. In a while, A purchases another tractor from C at a better price and trades in the tractor purchased from B for a car. B annuls the contract after A has performed the trade.

One can conclude that, pursuant to the DCFR, A must transfer the car if B demands it. Under the Law of Obligations Act, however, B can only demand the money, and, if A has no money to pay, A can offer the car to B by way of substitution. The solution offered by the DCFR is insufficiently flexible in the event that A would rather pay the money but B does not agree to this. The regulation in the Law of Obligations Act puts A in a more difficult situation in the case when A has no money and B refuses substitute performance.

2.4.2. Approval of disposal

If the enriched person has transferred the object received without legal basis, then, pursuant to Article VII.–5:101 (3), this constitutes a situation in which the enriched person is no longer able to transfer the asset in kind and has to pay its monetary value to the disadvantaged person. Upon disposal of an object in good faith, without charge, to a third person, the recipient may have a defence regarding disenrichment (Art. VII.–6:101), and the transferor has a claim against the third person pursuant to Article VII.–4:103, paragraph 2 of which establishes that a claim can be filed against a third person in particular in the event of disenrichment.

Pursuant also to Estonian law, a claim for transfer appears against a third party if the recipient transfers that which is received to a third party without charge and if compensation cannot be obtained from the recipient (§ 1036); the wording of the act does not expressly indicate that the impossibility of obtaining compensation should be confined to the case of reversal of enrichment. It is indicated in legal discourse that future judicial practice shall determine whether § 1036 shall be applied also if the performer of the disposal is insolvent. The wording of the DCFR allows one to presume that the insolvency of the performer of the disposal fails to justify the transferor's claim of unjustified enrichment and that the claims of the creditors of the insolvent debtor should be satisfied pursuant to the provisions of bankruptcy law. In any event, this is among the questions in consideration of which Estonian jurists and applicants of the law could make good use of the publishing of thorough DCFR comments.

In the case that the transfer of an object to a third person has been performed by an intervener in the rights of that person, both the DCFR (VII.–4:106) and the Law of Obligations Act (§ 1037 (2)) provide the possibility of the entitled person approving of the disposal and thus renouncing the thing involved.

Example: A steals B's car and sells it to C. B can demand C's return of the car or approve of A's disposal and demand the transfer of the money received for the car.

If a violator transfers the object to a third party without charge, that third party shall transfer what is received to the entitled person even if the right of disposal is valid (§ 1040).

2.4.3. Calculation of compensation

The basis for calculation of the amount of compensation for that which is received in the DCFR is as follows: pursuant to Article VII.–5:103, the monetary value of an enrichment is the sum of money which a provider and recipient with a real intention of reaching an agreement would lawfully have agreed as its price.

Pursuant to Estonian legislation, if it is impossible to deliver that which is received and in the event of violation of rights, the recipient shall compensate for the usual value (LOA, § 1032 (2) and § 1037 (1)) thereof, which, pursuant to the second sentence of subparagraph 65 of the General Part of the Civil Code Act, is the average local selling price (market price) of the object. In the case of disposal of an object by a violator for a charge, the agreed charge shall be deemed to be the usual value unless the entitled person proves that the value of the object is higher or the violator proves that the value of the object is lower than the agreed charge (§ 1037 (3)).

In its handling of a claim for compensation, the definition used in the DCFR converges with contract law applicable in the case of unjustified performance; whether this is justified remains questionable. This also complicates the determination of price, especially if the contract between the parties is void because of misrepresentation or threat. It proceeds from paragraphs 3 and 4 of Article 5:102 that a price fixed in a void contract is not applied so as to increase liability of the recipient beyond the monetary value of the enrichment, but, as is apparent from Article VII.–5:103, the monetary value still calls for assumptions regarding the real intention of the parties. If the parties disagree on the compensation payable or never entered into a contract in the first place, it would probably be difficult to ascertain what their real intention could have been. Therefore it would be more purposeful to use more objective criteria.

In the event of so-called imposed enrichment (i.e., the person did not consent to the enrichment), Article VII.–5:102 (2) (a) of the DCFR foresees that the enriched person is not liable to pay more than any saving.

This can be compared with § 1042 (2) of the Law of Obligations Act, establishing that a person who incurs costs with regard to an object of another person has no right of claim if the person with regard to whose object costs are incurred has contested the incurring of the costs in advance. This does not apply for necessary expenses (going toward preserving an object or to protect it against full or partial destruction) — reimbursement of these can be demanded pursuant to § 88 of the Law of Property Act⁶⁹. The DCFR thus does not distinguish as to the purpose of the expenses, but it might be presumed from the existing wording that what is meant is necessary expenses and not expenses the purpose of which is to increase the beauty or comfort of a thing.

2.5. Fruits

Article VII.–5:104 of the DCFR establishes that reversal of enrichment extends to the fruits and use of the enrichment or, if less, any saving resulting from the fruits or use; however, if the enriched person obtains the fruits or use in bad faith, reversal of the enrichment extends to the fruits and use, even if the saving is less than the value of the fruits or use. The wording of the DCFR article leads to the conclusion that it constitutes a principle by which an enriched person who is in good faith must transfer the benefit (fruits and use) actually received because of enrichment, whereas the liability of an enriched person who is in bad faith also comprises the fruits and uses that person might have received in consequence of enrichment.

This principle does not expressly proceed from the wording of the relevant provisions (sentence 1 of § 1032 (1) and also § 1035 (3) 1)) of the Law of Obligations Act, but, following the example of the DCFR, the act could also more clearly distinguish between these two situations.

When calculating the amount of fruits, Estonian judicial practice proceeds from the concept of usual value⁷⁰; with regard to Article VII.–5:104 of the DCFR, the question arises of whether the calculation of fruits should proceed from the same criterion foreseen for the calculation of the price of the object (i.e., proceeding from the presumed intention of the parties to the obligation, not the market price). If this is so, it gives rise to another question: that of whether this approach is justified in practice. I dare to claim that, with regard to determining the value of the object and of the fruits thereof, Estonian unjustified enrichment law provides a better and simpler solution than the DCFR.

⁶⁹ Asjaõigusseadus. – RT I 1993, 39, 590; 2007, 24, 128 (in Estonian); available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (20.08.2008).

⁷⁰ CCSCd 3-2-1-136-05, 20.12.2005, p. 26. – RT III 2006, 2, 19 (in Estonian).

3. Conclusions

As the DCFR was presented to the European Commission only at the end of 2007, comprehensive analyses related to the model rules of unjustified enrichment have not yet been published, for obvious reasons. The existing approaches that were available for use in preparation of the present article take a rather critical stance toward the model rules — they question the necessity of the separate regulation of unjustified enrichment altogether or at least question the necessity for such detail in this regulation, be it for the reason that it constitutes residual law or because of the excessively abstract and technical nature of the model rules developed thus far.^{*71}

The purpose of this article was to compare certain aspects of the unjustified enrichment regulation within the DCFR and the Estonian Law of Obligations Act. The assessment concluded that for the Estonian legislator the DCFR's unjustified enrichment model rules with their soon-to-be-published comments could prove helpful in addressing several questions in supplementing legislation and interpretation by means of judicial practice — for instance, in tackling the questions of law applicable to void contracts for provision of services, delimitation of *negotiorum gestio* and unjustified enrichment, or disposal of an insolvent debtor without charge. In addition, attention has been drawn to situations wherein the regulation of the Law of Obligations Act offers a more readily obtainable solution — for instance, determining the amount of compensation payable by the enriched person and determining the value of fruits derived from the object.

There is no need for restructuring of Chapter 52 of the Law of Obligations Act according to the example of the classification of unjustified enrichment claims in the DCFR. With regard to different types of enrichment, the Estonian legislator has considered it important to distinguish the regulation of prerequisites for claims from that addressing the extent of compensation (the performer's awareness of the lack of legal basis, as discussed in section 2.3.1, above, with consideration of additional prerequisites in compensating for the costs incurred addressed in section 2.4.3). Crossing over to a unitary approach would entail using rules with a more complex structure, establishing a multitude of exceptions, and making exceptions to those exceptions. In comparison of the provisions in question, a certain discontinuity of the DCFR text became evident, in failure to indicate whether the three functions of the DCFR should apply to the entire text or to its parts separately — the unjustified enrichment regulation occasionally repeats principles already included in Book III of the DCFR (as discussed in this paper's section 2.4.1).

Nonetheless, the DCFR undoubtedly plays an important role in teaching and research work in Estonia and elsewhere, as it evokes discussions regarding European private law, which delve into topics such as the existence of common elements and the scope of unjustified enrichment law.

⁷¹ See J. Smits (Note 31) and C. Wendehorst (Note 39).



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Shareholder's Derivative Claim — Does Estonian Company Law Require Modernisation?^{*1}

1. Shareholder of a public limited company — merely an investor or also a vigilant guard?

Whether and to what extent a member or shareholder should be able to influence the organisation as a whole is one of the most general conceptual issues in the development of company law provisions.^{*2} The nature and protection of shareholders' rights are closely related to the question of whether and to what extent shareholders as the providers of certain resources to the company should have the right to check the use of these resources.^{*3} One of the ways to answer this question is that a shareholder's rights with respect to the company should indeed be limited, because a public limited company is led by the directing bodies (directly or indirectly) elected by the shareholders and the company should be protected from shareholders' excessive interference. This approach is based on the premise that a shareholder is, first and foremost, an investor — they deliver funds to the company, expecting to gain profit over time. On the one hand, the directors of a company are relatively independent agents acting in the interests of the shareholders; on the other hand, the shareholders should have some kind of control over the directors.^{*4} To counterbalance the agency theory, it is stressed that a shareholder should be interested in the functioning of the company as a whole and this interest should not be limited to financial aspects, as the company's assets belong to an independent person — the public limited company.^{*5} However, it is a common view these days that in well-organised corporate governance, the shareholders, as the company's residual claimants^{*6} should have at their disposal an effective means of influencing the company's

¹ The article was published with support from ESF grant No ETF7297 "Theoretical Bases of the Harmonisation of Main Institutes of Civil Law in Europe and Its Impact on Civil Law and Legislation in Estonia".

² M. Habersack. Die Aktionärklage – Grundlagen, Grenzen und Anwendungsfälle. – Deutsches Steuerrecht 1998/14, p. 533.

³ T. Laurer. US – Corporate Governance während einer feindlichen Übernahme – oder "der Revlon Auslöser". – Zeitschrift für Vergleichende Rechtswissenschaft. Archiv für Internationales Wirtschaftsrecht. 103. Band. August 2004, p. 317.

⁴ K. M. Eisenhardt. Agency Theory: An Assessment and Review. – Theories of Corporate Governance: The Philosophical Foundations of Corporate Governance. T. Clarke (ed.). Oxon 2004, p. 79.

⁵ E. Ferran. Company Law and Corporate Finance. New York 1999, p. 315.

⁶ A residual claimant is a person whose right to receive back the sum invested in the company is granted in the last order, after the claims of all (other) creditors have been met.

activities when necessary.^{*7} For example, it is noted in Winter's report^{*8} that as shareholders focus on wealth creation, they are very suited to act as "watchdogs" who act not only on their own behalf, but also on behalf of other stakeholders. It has been noted in legal literature that in response to the rather extensive powers of the directing bodies, restoring the role of the shareholders has recently come to light again in Europe, amongst other things in legal regulation.^{*9} Protection of shareholder rights has also been stressed in various European Union documents as a priority area.^{*10}

Where a majority shareholder finds that a member of a directing body of the company has infringed or is infringing his or her obligations, the shareholder can usually respond to the situation, at a minimum, by replacing the member of the directing body and thus ensuring the possibility of claiming damages on behalf of the company. A minority shareholder's possibilities to influence the directing bodies are minimal. In most Member States of the European Union (including Estonia), the law vests special protective rights in shareholders representing a certain amount of share capital; such rights include the right to call the general meeting, to request a special audit, and other minority rights.^{*11} These are some of the most common ways for minority shareholders to intervene. The shareholders' right to claim damages on behalf of the company from a member of a directing body is a much less common legal remedy, which is not available under the company law of all countries. Usually it is the Anglo-American legal system that affirms the possibility of the shareholders' derivative claim, while in continental Europe the attitude to the permissibility of such intervention has been rather reserved.

The extent of harmonisation of company law has varied greatly in different areas; the main priorities in the protection of shareholders' rights have concerned the holding of general meetings and voting issues (such as the extension of possibilities of distance voting), also the right to receive information.^{*12} Even so, shareholders' intervention is now more regulated in many European countries than in Estonia. Major changes have also lately taken place in the regulation of derivative claims in the UK law, which is part of the Anglo-American legal system.^{*13} Thus, convergence is noticeable when it comes to the protection of shareholders' rights in the European Union, while the nature of the convergence is horizontal rather than vertical.

The objective of this article is to analyse the nature of derivative claims of shareholders' of a public limited company and the provisions and judicial practice concerning this legal remedy in various legal systems, particularly as exemplified by the USA, UK, and Germany. The subject is topical, amongst other reasons, because Germany has also gradually transposed and improved the regulation of derivative claims, while Estonia used the German example when devising the two-step management structure of public limited companies. The article seeks an answer to the question of whether Estonian company law would require modernisation, as the rights of shareholders, including minority shareholders, are being enhanced in Europe.

2. Concept and meaning of derivative claim

There is a contract-like relationship under the law of obligations between a member of a directing body and the company; of all the existing types of contracts, this relationship stands closest to an authorisation relationship.^{*14} Therefore, a member of a directing body will primarily have obligations to the company as the quasi-mandator. The legal remedies arising from an obligation (including rights of claim) are, however, rela-

⁷ P. Ireland. *Company Law and the Myth of Shareholder Ownership*. – International Themes in Business Law. S. Hardy, M. Butler (ed.). Vol. 2. Part III: Shares and Ownership, Shareholders. London 2007, p. 43.

⁸ Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company law in Europe. Brussels, 4.11.2002. Available at http://ec.europa.eu/internal_market/company/docs/modern/report_en.pdf (21.11.2008).

⁹ L. Timmerman, A. Doorman. Rights of Minority Shareholder in the Netherlands. – Electronic Journal of Comparative Law, December 2002/6.4. Available at <http://www.ejcl.org/64/art64-12.pdf> (21.11.2008).

¹⁰ E.g., Commission of the European Communities. Communication from the Commission to the Council and the European Parliament. Modernising Company Law and Enhancing Corporate Governance in the European Union — A Plan to Move Forward. Brussels, 21.05.2003. COM(2003) 284 final. Available at http://www.ecgi.org/commission/documents/com2003_0284en01.pdf (21.11.2008); Directorate General for Internal Market and Services. Consultation on Future Priorities for the Action Plan on Modernising Company Law and Enhancing Corporate Governance in the European Union. Available at http://ec.europa.eu/internal_market/company/docs/consultation/consultation_en.pdf (21.11.2008), etc.

¹¹ About the different types and threshold of minority rights, see L. Timmerman, A. Doorman (Note 9).

¹² M. Kotkke. Harmonisierung der internen Struktur von Aktiengesellschaften – die europäische Empfehlung zur Unabhängigkeit der Direktoren und zu den Ausschüssen. Dissertation zur Erlangung der Doktorwürde. Augsburg, 2007, pp. 54–55. Available at http://deposit.d-nb.de/cgi-bin/dokserv?idn=987381342&dok_var=d1&dok_ext=pdf&filename=987381342.pdf (21.11.2008).

¹³ Canada, Australia, New Zealand, and the UK have now regulated the issue by law instead of the former common law regulation. See, e.g., A. Steinfeld, M. Mann, R. Ritchie *et al.* Blackstones Guide to The Companies Act 2006. Oxford 2007, p. 103.

¹⁴ The Supreme Court has understood the relationship between a management board member and the company in the same way. See CCSCd 26 April 2005, 3-2-1-39-05. – RT III 2005, 15, 155 (in Estonian).

tive — they pertain not to everyone, but to a specific person — the other party to the obligation.^{*15} In the same way, this right can usually be exercised only by the other party to the obligation (the entitled person), which is why in a situation where a member of a directing body infringes his or her obligation and causes damage to the company, it is the company that is entitled to assert a claim. However, a legal person is an artificial subject of law created by law,^{*16} which acts via its directing bodies, and this principle may preclude the assertion of a claim against a member of a directing body, if there is no mechanism to eliminate the infringer's possibility to influence the assertion of the claim. This problem arises especially sharply in the conflict between minority and majority,^{*17} because a majority shareholder can influence the violator (at least theoretically) via control of directing bodies. In addition, positive law usually creates a mechanism that takes the decision over the assertion of a claim "one step higher" (in the event of a two-step management structure, to the competence of the supervisory board or general meeting).

Due to the above, the company laws of many countries have extended the shareholders' right of interference and, in certain circumstances, allowed shareholders representing a certain proportion of share capital to file a claim for compensation in the courts against a member of a directing body who has infringed his or her rights. Such a legal remedy has been also called *actio pro socio* in legal literature. In the event of *actio pro socio*, a claim is not filed directly to protect the claimant's own right, but also the right of others (who are connected to him or her under company law or otherwise).^{*18} Therefore, the nature of the rights being protected differs from the rights protected by one's own claim: a derivative claim is mainly aimed at protecting the company's interests, while a shareholder's personal claim is only aimed at protecting the shareholder's own financial interests.^{*19} There is also a distinction based on whether the shareholders can only decide over the assertion of a claim or can actually file the claim independently. The latter case is the classic derivative claim: the claim is brought by a shareholder or shareholders, not by the company (via a representative elected by the shareholders), although it is the company which is sought to be compensated.^{*20}

Although the guarantee of shareholders' rights should be considered important, it has been mentioned in legal literature that giving shareholders an easy possibility of claim could lead to a situation where groups of displeased shareholders would disturb the company's operations with their constant claims and thus reduce shareholder value.^{*21} This is why the possibilities for such claims are limited even in those legal orders that allow for derivative claims.

3. Legal regulation of derivative claims in the company law of various countries

As mentioned above, different legal orders have different approaches to the position of shareholders in a company and hence the legal remedies afforded to them. It has even been argued in literature that the degree of protection of shareholders' rights varies a great deal depending on the legal system or family of law. A group of economists led by Rafael La Porta, Florencio Lopez-de-Silanes, and other authors have noted in their series of articles titled "Law and Finance",^{*22} which evoked responses from many legal scientists, that common law countries offer better shareholder protection than continental Europe.^{*23} It is, of course, true that in German company law, the structure of directing bodies is mainly based on the theory of independent

¹⁵ H. Köhler. Tsiviilseadustik. Üldosa (Civil Code. General Part). Tallinn 1998, pp. 30–31, marginal 11 (in Estonian).

¹⁶ For more details about the content of the legal subjectivity of a legal person in private law see K. Saare. Eraõigusliku juriidilise isiku õigus-subjektsuse piiritlemine. Doktoritöö (Delimitation of the Legal Subjectivity of a Legal Person in Private Law. Doctoral Thesis). Tartu 2004 (in Estonian).

¹⁷ A limited liability company inevitably entails sources of conflict between different types of interest groups, and the second most common conflict besides that between the owner and the manager is the conflict of interests between majority and minority shareholders. For detailed discussion, see H. Hansmann, R. Kraakman. Agency Problems and Legal Strategies. – The Anatomy of Corporate Law. A Comparative and Functional Approach. R. Kraakman *et al.* (ed.). Oxford 2004, p. 21.

¹⁸ C. Griebler. Die zivilrechtliche und strafrechtliche Haftung eines geschäftsführenden Organs einer Tochtergesellschaft bei „upstream securities“ im Konzern nach schwedischem und nach deutschem Recht. Dissertation zur Erlangung der Doktorwürde. Bremen 2006, p. 52.

¹⁹ M. Habersack (Note 2), pp. 533–535.

²⁰ *Ibid.*, p. 533.

²¹ See D. Bradford. Shareholder Derivative Suits: A Growing Concern for Corporate Directors and Officers. – Advisen. Insight for Insurance Professionals, July 2005. Available at http://www.cnapro.com/pdf/ShareholderDerivativeSuits_Advisen.pdf (21.11.2008).

²² R. La Porta, F. Lopez-de-Silanes, A. Shleifer, R. Vishny. Law and Finance. – Journal of Political Economy, December 1998 (106) 6. Available at <http://mba.tuck.dartmouth.edu/pages/faculty/rafael.laporta/publications/LaPorta%20PDF%20Papers-ALL/Law%20and%20Finance-All/Law%20and%20Finance.pdf> (21.11.2008).

²³ U. C. Brändle. Shareholder Protection in the USA and Germany — "Law and Finance" Revisited. – German Law Journal 2006 (7) 03, pp. 257–278.

supervision, according to which an independent supervisory body is considered to be the best protector of the company's interests.^{*24} Udo Brändle has criticised the position of La Porta *et al.* and noted that although German company law has been somewhat more modest in allowing shareholders to intervene, one should not forget that shareholders representing 10% of the share capital were able to decide on the assertion of a claim on behalf of the company already before the aforementioned study was published.^{*25}

The main source of company law in the United Kingdom is the Companies Act 2006^{*26} (CA 2006), Part 11 of which governs derivative claims. These provisions were recently modernised: according to the amendments that entered into force on 1 October 2007, the former principle of admissibility of proceedings, which originated from the *Foss v. Harbottle* case, was replaced by a more flexible approach that allows for more rational and clearer identification of a shareholder's right to file a derivative claim.^{*27} The pre-reform check of admissibility of proceedings was based on two premises: firstly, the underlying violation had to be not approvable by a majority decision, and secondly, the violator's control of the company had to prevent the assertion of the claim.^{*28} The latter principle meant that where a majority of shareholders, independent of the violator, accepted the situation, a derivative claim was not admissible.^{*29} This is why *Foss v. Harbottle* did not allow for the actual protection of minority shareholders' interests.^{*30} As a result of the reform, CA 2006 provides that any shareholder may file a derivative claim regardless of the number of shares held by him or her, regardless of the nominal value of the shares and of when he or she acquired the shareholding. A claim can be filed against any current or former member of a directing body, as well as against a shadow director^{*31}. The spectrum of violations in which case a derivative claim can be filed is also quite wide — both intentional and negligent breaches, and breaches of both duty and trust.^{*32} At the same time, doubts have been expressed in connection with the reform about whether such extension of shareholder rights together with the newly introduced express obligation of the directors to act in the best interests of the company would not lead to an excessive activism of shareholders and jeopardise the business judgement rule as the main guarantor of the directors' independence.^{*33}

In German company law, it is, as a rule, up to the supervisory board to decide on a claim against members of the management board (§ 111 of the *Aktiengesetz*^{*34} (AktG)); filing a claim for compensation for damage resulting from a breach of the duties of supervisory board members is within the competence of the management board (AktG § 78).^{*35} In addition, AktG § 147 allows the general meeting to decide on the filing of a claim against members of a directing body: according to subsection 1 of the aforementioned section, the general meeting usually decides on the filing of such a claim by simple majority.^{*36} A claim has to be filed with a court within six months of the general meeting's decision. According to AktG § 147 (2), the general meeting may appoint a special representative of the company, if necessary, for the assertion of the claim. Such regulation has been in force in Germany for a long time, while German company law has lately also taken a considerable step toward extending the rights of shareholders.^{*37} After intensive discussions^{*38}, the *Bundestag* adopted on

²⁴ A. F. Conard. The Supervision of Corporate Management: A Comparison of Developments in European Community and United States Law. — Michigan Law Review 1984 (82), pp. 1464–1467.

²⁵ U. C. Brändle (Note 23), pp. 272–273.

²⁶ Available at http://www.opsi.gov.uk/ACTS/acts2006/ukpga_20060046_en.pdf (21.11.2008).

²⁷ B. Hannigan. The Derivative Claim — an Invitation to Litigate? — Hannigan and Prentice: The Companies Act 2006 — A Commentary. B. Hannigan, D. Prentice (ed.). Butterworths, London: LexisNexis 2007, p. 65.

²⁸ It should be noted that common law also considers the company itself the first most appropriate plaintiff in the event of a claim for damages against a director.

²⁹ There were a few exceptions to this general rule, for example the majority's protection was precluded in the event of a fraud against the minority.

³⁰ G. Morse. Charlesworth's Company Law. G. Morse, S. Girvin *et al.* (ed.). 17th edition. London 2005, pp. 337–338.

³¹ The Estonian law is not familiar with the concept of a shadow director; the closest institute, with certain reservations, is constituted by the persons influencing the activities of a public limited company as specified in § 289² of the Commercial Code, whose liability was set out by an amendment to the Commercial Code that entered into force on 1 January 2006. It is planned to extend this regulation to the provisions governing private limited companies. In English law, the legal status of a shadow director has quite specific content. See, e.g., G. Morse (Note 30), pp. 269–270.

³² B. Hannigan (Note 27), p. 76.

³³ *Ibid.*, p. 68.

³⁴ Aktiengesetz vom 6. September 1965 (BGBl. I S. 1089), zuletzt geändert durch Artikel 11 des Gesetzes vom 16. Juli 2007 (BGBl. I S. 1330). Available at <http://bundesrecht.juris.de/bundesrecht/aktg> (21.11.2008).

³⁵ W. Bayer. Aktionärsklagen *de lege lata* und *de lege ferenda*. — Neue juristische Wochenschrift 2000/36, p. 2613.

³⁶ This provision governs not only claims for compensation for damage against members of a directing body, but also against founders and other persons, e.g., persons who have contributed to damaging the company intentionally or by gross negligence upon transfer of assets to the company upon the company's foundation (AktG §§ 46 and 47). The regulation also governs ex-post incorporation (AktG § 53).

³⁷ M. M. Siems. Welche Auswirkung hat das neue Verfolgungsrecht der Aktionärminderheit. — Zeitschrift für Vergleichende Rechtswissenschaft. Archiv für Internationales Wirtschaftsrecht. 104. Band. August 2005, p. 376.

³⁸ G. Spindler. Haftung und Aktionärsklage nach dem neuen UMAG. — Neue Zeitschrift für Gesellschaftsrecht 2005/21, p. 865.

15 June 2005, an act regulating the integrity of companies and the modernisation of the right of contestation (*Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts*^{*39}), which entered into force on 1 November 2005, and has been called the most important reform of the German company law since 1965.^{*40} Among other things, the act supplemented *Aktiengesetz* with § 148, under which shareholders representing the certain amount of share capital are entitled under certain conditions and in lieu of the company to assert claims for compensation for damage against members of directing bodies.

In order to file a claim, the shareholder or shareholders are required to represent 1/100 of the share capital or hold shares corresponding to € 100,000 of capital. After a claim is filed, its admissibility is first assessed. As the first prerequisite of admissibility, the shareholders must have acquired the qualifying shareholding before they learned about the underlying circumstances of the claim. This is to prevent later acquisition of shares for the purpose of asserting a claim. Secondly, it has to be proved that the shareholders have, during a reasonable time, unsuccessfully requested the company itself to file a claim for damages. Thirdly, there have to be circumstances justifying the suspicion that the company has been damaged by gross violation of law or the articles of association or by unfair play, and fourthly, the claim must not be contrary to the company's interests or constitute an excessive burden on the company. According to AktG § 148 (4), if the court has found the claim to be admissible, the claim has to be filed within three months after the entry into force of the court's decision. Further simultaneous disputes by other shareholders or the company itself are precluded. Also important are the rules, according to which a decision made in such a proceeding is binding on both the company and all of its shareholders, and a listed company has to disclose the admissibility of the claim and the result of the proceedings.

This indicates a trend toward enhanced shareholder protection in the two influential European countries that offer principally different legal solutions in company law as well as several other fields of private law. When assessing the importance of the German reform, we should take into account, among other things, the special structure of German public limited companies: the formation of a supervisory board is a rather indirect way for even majority shareholders to exercise influence.^{*41}

Of the non-European countries representing the Anglo-American legal system, the Delaware General Corporation Law^{*42} is an example of minimal legal regulation of shareholders' derivative claims; § 327 of the Law only provides for the basic rule: in any derivative suit instituted by a stockholder of a corporation, it shall be averred in the complaint that the plaintiff was a stockholder of the corporation at the time of the transaction of which such stockholder complains or that such stockholder's stock thereafter devolved upon such stockholder by operation of law. The conditions and procedure for derivative suits is addressed in more depth in the US Model Business Corporation Act, §§ 7.40–7.47 of which stipulate the exact prerequisites and limitations of such actions and the procedure rules.^{*43}

The example of French law should be pointed out from continental Europe. Article L225–252 of the *Code Commerce*^{*44} provides for the shareholders' right to bring an action for liability on behalf of the company against its directors or managing director; further representation requirements apply to listed companies under article L225–120 (individual shareholders cannot file a claim; the rate of representation varies slightly depending on the size of the company's share capital).

Thus, it may be said that the possibility of filing a derivative claim is nowadays one of the statutory remedies of shareholders in a large number of countries.

³⁹ Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts v 22.09.2005. Bundesgesetzblatt Jahrgang 2005, Teil I, Nr 60. Available at <https://www.ebundesanzeiger.de/download/bgb1105s2802.pdf> (21.11.2008).

⁴⁰ G. Spindler (Note 38), p. 865.

⁴¹ AktG § 96 provides for five different methods of setting up a supervisory board depending on whether and to what extent the rules of employee involvement apply to the company; in many public limited companies, only a minority of supervisory board members are appointed by shareholders. Employee involvement is regulated in Germany mainly (but not only) by the Employee Involvement Act: *Gesetz über die Mitbestimmung der Arbeitnehmer* (Mitbestimmungsgesetz) vom 4. Mai 1976 (BGBl. I S. 1153), zuletzt geändert durch Artikel 18 des Gesetzes vom 14. August 2006 (BGBl. I S. 1911). Available at <http://www.gesetze-im-internet.de/mitbestg/index.html> (21.11.2008).

⁴² Available at <http://delcode.delaware.gov/title8/c001/index.shtml> (21.11.2008).

⁴³ Model Business Corporation Act Annotated, 2005, 4th edition. Available at <http://www.abanet.org/buslaw/committees/CL270000pub/nosearch/mbca/assembled/20051201000001.pdf> (21.11.2008).

⁴⁴ *Code de Commerce* (Commercial Code). Last amendment: Act No. 2006-11 of 5 January 2006 Art. Official Journal of 6 January 2006. Available at <http://195.83.177.9/code/liste.php?lang=uk&c=32> (21.11.2008). The provisions discussed in this paper are from the year 2001, so that the English wording can be used regardless of the older version.

4. Judicial practice in derivative claims and related issues

The main economic problem concerning derivative claims is the reduction in shareholder value as a result of a dispute. From the legal-economic viewpoint, a shareholder would rather be encouraged to sell his or her shares if the shareholder's rights are violated, and not burden himself or herself and the company with a time-consuming lawsuit. The US insurance corporation Advisen Ltd.⁴⁵ has analysed the decisions taken in derivative actions during the period 1993–2005, and found that there is an upward trend in the number of derivative action rulings. About half of derivative actions end with decisions in favour of defendants. Only few cases result in monetary relief, while the values are typically relatively low; however, the company always incurs huge legal costs. Therefore, it has been opined that derivative claims and related lawsuits benefit only the legal advisers involved.⁴⁶

One of the questions that arises in company law, time and again, is to what extent the values of company law (which are largely material values, though with a much broader meaning) should be protected by private law remedies, and whether the provisions of other branches of law, especially penal law, should be used to solve certain problems.

Franklin Gewurtz has conducted an in-depth analysis of two remarkably similar cases of director's liability from two countries representing different legal systems — the United States and Germany.⁴⁷ In both cases, such large severance payouts were made to directors that it caused doubts as to the legitimacy of the payouts. The US case studied was *In re The Walt Disney Company Derivative Litigation* in the Delaware Chancery Court as the court of first instance and the Delaware Supreme Court as the court of appeal.⁴⁸ The shareholders of Disney brought a derivative action and demanded compensation from directors for the damage done to the company by the payment of an excessive severance payout to one of the directors.⁴⁹ As a result of a lengthy and arduous litigation, the court decided that there was no ground for compensation, because the company did not actually suffer loss.

The compared German case was the case of *Mannesmann*, in which the members of the supervisory board awarded and paid an excessive bonus to an outgoing director and criminal proceedings were brought against them on the grounds of breach of fiduciary duty (*Untreue*).⁵⁰ It should be noted here that similar grounds were introduced to the Estonian Penal Code⁵¹ by an amendment that entered into force on 15 March 2007; § 217² (1) of the Penal Code now defines abuse of trust as illegal use of the right arising from law or transaction to dispose of assets of another person or assume obligations for another person, or violation of an obligation to comply with the financial interests of another person if such act results in major damage but does not contain the necessary elements of an embezzlement.⁵²

The Düsseldorf County Court, as the court of first instance, found that the directors were indeed in breach of their duty when awarding the bonus, but as according to the law, breach of fiduciary duty means causing significant damage to another person's financial interests, and the company was making a profit at the time of the award and the breach did not damage the company's financial situation, the act of the directors did not contain the necessary elements of *Untreue*. The German Supreme Court (*Bundesgerichtshof*) did not agree with the position of the court of lower instance and found that *Untreue* does not necessarily require significant damage to the company's financial interests.⁵³ The case was referred back to the county court, but an agreement was reached before the case was heard again: namely, the directors agreed to pay a sum of € 5.8 million and the case was closed.

⁴⁵ About the background of the New York-based Advisen Ltd., see their Web site <https://www.advisen.com/company.html> (21.11.2008).

⁴⁶ D. Bradford (Note 21).

⁴⁷ F. A. Gewurtz. Disney in a Comparative Light. SSRN Electronic Paper Collection. 26.02.2007, pp. 1–38. Available at <http://ssrn.com/abstract=965596> (21.11.2008).

⁴⁸ Decision of the Delaware Supreme Court of 8 June 2006. *In re The Walt Disney Company Derivative Litigation* No. 411, 2005. Available at [http://courts.delaware.gov/opinions/\(wqdsib55g41131ajtaxpls55\)/download.aspx?ID=77400](http://courts.delaware.gov/opinions/(wqdsib55g41131ajtaxpls55)/download.aspx?ID=77400) (21.11.2008).

⁴⁹ If we compare the directing bodies of an American public limited company with a company with a two-step management structure, the board is rather like the supervisory board and the Chief Executive Officer is a director who manages daily operations. About the management structure of US companies in greater detail, see M. Vutt. *Aktiaseltsi juhtimismudeli õiguslik reguleerimine*. Magistritöö (Legal Regulation of the Management Model of a Public Limited Company. Master's Thesis). Tartu 2006, pp. 27, 32–33 (in Estonian).

⁵⁰ Decision of the Federal Supreme Court of 21 December 2005: BGH (*Bundesgerichtshof*), 21.12.2005 – 3 StR 470/04. – *Neue Juristische Wochenschrift* 2006, p. 522.

⁵¹ *Karistusseadustik*. Adopted on 6.06.2001. – RT I 2001, 61, 364; 2007, 31, 187 (in Estonian).

⁵² According to § 201 of the Penal Code, embezzlement means illegal conversion by a person into his or her use or the use of a third person movable property which is in the possession of another person or other assets belonging to another person which have been entrusted to the person.

⁵³ § 266 (1) of the German Penal Code (*Strafgesetzbuch*) generally defines breach of fiduciary duty as the abuse of another person's right to dispose of property (regardless of the legal basis of disposal) or the abuse of the duty to consider another person's proprietary interests and thereby causing damage to the other person's proprietary interests.

Gewurtz reached an interesting result when comparing the two cases: although the application of director's liability (especially when initiated by shareholders) seemed, at first glance, to be easier under the law of Delaware, it was the German case that ended with a decision deploring the directors' award of the excessive bonus, while the directors of Disney were fully exonerated regardless of their not exactly best practice of corporate governance, as referred in the court decision.^{*54} Gewurtz found that such a result may be partly due to different types of proceedings: on the one hand, government prosecutors may well enjoy greater credibility than plaintiffs' attorneys, who make a business out of bringing derivative suits on behalf of shareholders; on the other hand, the criminal court is less experienced in matters of civil law, especially company law, which is why there is less space for discretion from the viewpoint of the business judgement rule.^{*55} In any case, the example described above leaves the impression that the German criminal court disregarded the warning that in the event of directors' decisions, a negative consequence (in this case, reduction of the company's assets, although its financial status did not suffer) does not automatically imply mismanagement.^{*56} In legal terms, both the directing body's mistake and the damage have to be proved separately.

Gewurtz correctly notes that the absence of civil law alternatives or major obstacles to the application of such alternatives render criminal prosecution the only realistic alternative of exercising one's rights.^{*57} It is questionable whether such one-sidedness of legal remedies is correct and serves the interests of a company's stakeholders. The author of this article believes that penal mechanisms cannot be overestimated and that one remedy cannot fully replace another.

It may be concluded from the above that also in the countries where derivative actions have been regulated for a long time, actual lawsuits and the application of directors' liability are not especially common.^{*58} Nevertheless, or perhaps even because of that, the legislatures of various countries have attempted to instead enhance the rights of shareholders. It is therefore justified to ask whether Estonian company law could benefit from new solutions.

5. Would Estonia need modernisation of shareholder rights and the legalisation of derivative claims?

The Estonian Commercial Code (CC) provides for a limited competence of shareholders of public limited companies. CC § 298 (1) lists the competence of the general meeting in nine points and adds, as the tenth point, that the general meeting is competent to decide on other matters placed in the competence of the general meeting by law. A general meeting may adopt resolutions on other matters related to the activities of the public limited company on the demand of the management board or supervisory board (CC § 298 (2)). This is the "non-interference" principle, the aim of which is to ensure that a company as an independent legal person acts independently of its shareholders; among other things, it also means subjection to the "majority decides" rule.^{*59} The situation where a company can act without judicial, and also without excessive legislative interference, has been considered to be a guarantee of the company's continuity.^{*60} Voting at the general meeting would then remain a shareholder's basic possibility to express his or her wishes and attitudes.^{*61}

According to CC § 317 (8), the supervisory board shall decide on the conduct of legal disputes with members of the management board and shall appoint a representative of the company for the conduct of such disputes. In the creation of the Estonian legal framework for companies, it has been considered sufficient that the role of the supervisory board as an autonomous supervisory body ensures (especially if the supervisory board members are independent) an appropriate mechanism for filing a claim against a member of the management board. It is the general meeting of shareholders which is competent to decide on the filing of a claim against

⁵⁴ It has been mentioned in literature that the court clearly distinguished between "making a bad decision" and "damaging the company", which indeed is not the same from the company law viewpoint. See: The rights and wrongs Ovitz. – *Economist*, 13 August 2005 (Vol. 376 Issue 8439), pp. 50–51 (Academic Search Premier).

⁵⁵ F. A. Gewurtz (Note 47), p. 37.

⁵⁶ F. H. Easterbrook, D. R. Fischel. *The Economic Structure of Corporate Law*. Cambridge 1998, p. 99.

⁵⁷ F. A. Gewurtz (Note 47), p. 36.

⁵⁸ Even in the USA it is noted that shareholders' democracy is a myth rather than reality. See, e.g., Keeping shareholders in their place. – *Economist* 13 October 2007 (Vol. 385 Issue 8550), pp. 69–70. (Academic Search Premier). Available at http://www.economist.com/business/displaystory.cfm?story_id=9961252 (21.11.2008).

⁵⁹ R. Redmond-Cooper. *Management Deficiencies and Judicial Intervention: A Comparative Analysis*. – *International Themes in Business Law*. S. Hardy, M. Butler (ed.). Volume 2. Part III: Shares and Ownership, Shareholders. London 2007, p. 155.

⁶⁰ J. Rickford. *Fundamentals, Developments and Trends in British Company Law – Some Wider Reflections*. First Part: Overview and the British Approach. – *European Company and Financial Law Review*, December 2004 (1) 4, p. 402.

⁶¹ G. Morse (Note 30), p. 337.

a supervisory board member, but since the law prescribes a majority requirement, the possibility that a 10% shareholder could assert such a claim is almost zero.

This problem has similarities to German law: Manuel Rene Theisen and Wolfgang Salzberger noted in 2002, that since World War II, not a single civil claim for damages had been asserted against a member of a supervisory board in Germany.^{*62} At least one of the reasons for this undoubtedly lies in the supervisory board's specific role in the two-step management structure of a public limited company. As daily operations are managed by the management board, it is the management board's activity that influences the company's status either positively or negatively. It may thus be assumed that shareholders are probably not so much interested in gaining control of the supervisory board as they are interested in asserting claims against members of the management board.

In summary, it may be said about Estonian company law that the Commercial Code protects shareholders mainly by an *ex-ante* strategy^{*63}: the few existing remedies are aimed at preventing breaches rather than responding to the consequences of breaches. At the same time, application of the *ex-ante* or preventive strategy requires a majority-based influence on the directing bodies of a company, which is why it is usually not available to minority shareholders.

An analysis of the judicial practice of claims against members of directing bodies of companies in Estonia shows that such claims are filed mainly in bankruptcy proceedings.^{*64} It is quite difficult to establish and prove the evidence on which a claim is based (especially the damage and the causation), and proceedings often end in a compromise.^{*65} The specific nature of bankruptcy proceedings is inevitably transferred to the litigations held on behalf of a bankrupt company: as such proceedings are held with limited resources, the result may largely depend not only on the legal justification, but on whether the creditors of the bankrupt company have the possibilities and desire to "support" the litigation of a claim. Considering that creditors have already incurred damage due to bankruptcy and are not likely to risk further damage, claims for damages against members of a directing body have little success when the company is bankrupt.

This leads to the hypothesis that if the law provided for an adequate mechanism for earlier intervention, it would be somewhat easier to establish the grounds of the claim, because the difficulties of asserting a claim are certainly influenced by the complicated causal chains, which are created over a longer period and under various economic influences, and the mutual relations of which are much more difficult to establish once the company is insolvent.^{*66}

Mentioned above were penal law measures as an alternative to civil liability, which is why this issue should also be discussed in the context of Estonian law. The explanatory memorandum to the draft amendment to the Penal Code^{*67}, which introduces the necessary elements of abuse of trust, states: "Abuse of trust is an offence against property which consists in the illegal use of the right to dispose of another person's assets or to assume obligations for another person, or violation of the duty to comply with another person's financial interests, if such act results in major damage to such other person. For the purpose of these necessary elements of offence, major damage is to be incurred by the person whose financial interests the offender was to comply with, i.e., by the person whose trust is abused. The necessary elements of the offence are limited to major damage, since, as a rule, disputes arising on the basis of the right of representation could be settled by civil proceedings. [...] The wording of the necessary elements of the offence follows, among others, the examples of the German and Swiss civil codes (the German StGB § 266 and the Swiss StGB § 158)".

The necessary elements of abuse of trust in Estonian law are thus limited to the extent of damage — only an act resulting in major damage is regarded as abuse of trust. According to § 8 (1) of the Penal Code Implementation Act^{*68}, damage exceeding one hundred times the established minimum monthly wage is major damage.

⁶² M. R. Theisen, W. Salzberger. Germany's "Aufsichtsrat" board. Three ideas for the 'two-tier' approach. — Legamedia, February 2002. Available at http://www.legamedia.net/dy/articles/article_15789.php (21.11.2008).

⁶³ H. Hansmann, R. Kraakman. Agency Problems and Legal Strategies. — R. Kraakman *et al.* The Anatomy of Corporate Law. A Comparative and Functional Approach. Oxford 2004, pp. 27–31.

⁶⁴ In particular, see CCSCd 11 May 2005, 3-2-1-41-05. — RT III 2005, 17, 181; 25 April 2006, 3-2-1-27-06. — RT III 2006, 17, 162; 25 April 2006, 3-2-1-27-06. — RT III 2006, 17, 162; 15 May 2006, 3-2-1-36-06. — RT III 2006, 21, 195; 14 June 2006, 3-2-1-52-06. — RT III 2006, 24, 224 (all in Estonian).

⁶⁵ M. Vutt. Establishment of breaches of directing bodies' duties, including grave errors in management and criminal conduct in the practice of bankruptcy proceedings: Kohtupraktika analüüs (Analysis of Judicial Practice). Tartu 2008, pp. 3–4. Available at www.riigikohus.ee (21.11.2008) (in Estonian).

⁶⁶ Insolvency entails a cumulation of negative consequences, which is why the establishment of damages can be problematic, because in a bankruptcy situation, the negative consequence of a director's breach has to be distinguished from the overall body of negative consequences that led to the insolvency.

⁶⁷ Karistusseadustiku ja selle muutmise seaduse eelnõu seletuskiri. (Draft Act amending the Penal Code and related Acts. Explanatory Memorandum), 5.06.2006. Available at <http://web.riigikogu.ee/ems/saros-bin/mgetdoc?itemid=061590005&login=proov&password=&system=ems&server=ragne11> (21.11.2008) (in Estonian).

⁶⁸ Karistusseadustiku rakendamise seadus. Adopted on 12.06.2002 — RT I 2002, 56, 356; 2007, 13, 69 (in Estonian).

According to Government of the Republic Regulation No. 254 of 20 December 2007 “Establishment of the minimum monthly wage”⁶⁹, the minimum monthly wage for full-time work from 1 January 2008 is EEK 4350; the damage constituting a necessary element of abuse of trust is thus at least EEK 435,000.

Considerable problems may arise at the present time from the possible application of the principle of opportunity in criminal proceedings.⁷⁰ One of the expressions of the principle of opportunity is Guidance No. RP-1-4/07/3 of the Chief Public Prosecutor of 12 April 2007, which sets out the principles for following public interest in proceedings in the application of §§ 202, 203 and 203¹ of the Code of Criminal Procedure. According to article 49 of the Guidance, there is, generally, public interest in the case of § 217² of the Penal Code, but in the context of the additional criteria listed in article 6, it is not clear whether an initial public interest in the proceedings can disappear, e.g., because the injured party does not wish the proceedings to continue. It should be considered likely, taking into account that even in Germany, in the *Mannesmann* case, it was possible to end the proceedings by an agreement.

It follows from the above that the legal rights protected by penal law do not completely overlap with the rights that should be protected by private law. Therefore, one has to take the view that solely penal law mechanisms in Estonian law cannot be considered sufficient legal remedies to respond to the breaches of directing bodies.

Against the background of general tendencies toward balanced extension of shareholder rights in the European Union and elsewhere, one may ask to what extent the Estonian law is following the same trends. Recent changes in Estonian company law have not been remarkable. The provisions of the Commercial Code that entered into force on 1 January 2006 can be regarded as partly an additional introduction of the changes arising from the Law of Obligations Act, and partly as the codification of judicial practice. Later amendments have largely been “forced moves” caused by the transposition of various European Union rules. The amendments of 15 November 2006 arose directly from amendments to the Estonian Central Register of Securities Act⁷¹ and the need to provide for a detailed procedure for the exchange of information between the Estonian Central Register of Securities and the Commercial Register⁷²; the amendments of 6 December 2006 were necessitated by the implementation of the European Union guideline, according to which from the end of 2007, the founding of a company should not take more than a week;⁷³ the amendments of 15 December 2007 introduced the provisions of cross-border merger⁷⁴ and the amendments of 20 March 2008 transposed the directive amending the Capital Requirements Directive.⁷⁵ The extension of shareholder rights has not been much talked about, because there has been no direct pressure to make legislative changes. Still, there is the question of whether a shareholder of an Estonian public limited company, including a minority shareholder, does not need remedies comparable to those available in other European countries. The question is not only about a narrow legislative choice, but about a more general emphasis based on the shaping of the investment environment.⁷⁶

Although one should agree with the view that, e.g., the harmonisation of various procedural laws⁷⁷ could be one of the development directions among others, it is only a thought which is so far not expressed by the reality of law. This is why support should be given to legislative drafting that contributes to the development of independent private law remedies. In this light, it should be admitted that the inner structure of an Estonian public limited company is very strongly supportive of the autonomy of directing bodies — while, e.g., AktG § 119 allows for extending the competence of the general meeting at the expense of the competence of the supervisory board (but not the management board) by the articles of association, Estonian law does not allow for such extension. Such a great degree of autonomy should be at least partly balanced by appropriate remedies available to shareholders.

⁶⁹ Palga alammäär kehtestamine. – RT I 2007, 71, 442 (in Estonian).

⁷⁰ For details about the principle of opportunity see, e.g., K. Savtšenkova. *Kriminaalmenetluse lõpetamine süü väikuse ja avaliku huvi puudumise tõttu oportuuniteedi põhimõtte väljendusena*. Magistritöö (Termination of Criminal Proceedings due to Negligibility of Guilt and Lack of Public Interest as an Expression of the Principle of Opportunity. Master's Thesis). Tartu 2007 (in Estonian).

⁷¹ Eesti väärtpaberite keskregistri seadus. Adopted on 14.06.2000. – RT I 2000, 57, 373; 2007, 12, 66 (in Estonian).

⁷² Eesti väärtpaberite keskregistri seaduse ja äriseadustiku muutmise seadus (Estonian Central Register of Securities Act and Commercial Code Amendment Act). Adopted on 15.11.2006. – RT I 2006, 55, 407 (in Estonian).

⁷³ Äriseadustiku muutmise ja sellega seonduvalt teiste seaduste muutmise seadus (Commercial Code and Related Acts Amendment Act). Adopted on 6.12.2006. – RT I 2006, 61, 456 (in Estonian).

⁷⁴ Äriseadustiku ja sellega seonduvate seaduste muutmise seadus (Commercial Code and Related Acts Amendment Act). Adopted on 15.12.2007. – RT I 2007, 65, 405 (in Estonian).

⁷⁵ Äriseadustiku ja Euroopa Liidu Nõukogu määruse (EÜ) nr 2157/2001 „Euroopa äriühingu (SE) põhikirja kohta” rakendamise seaduse muutmise seadus“ (Act Amending the Commercial Code and Council Regulation (EC) No. 2157/2001 on the Statute for a European company (SE) Implementation Act). Adopted on 20.03.2008. – RT I 2008 16, 116 (in Estonian).

⁷⁶ M. Käerdi, R. Lang, J. Raidla, P. Varul, U. Volens. Ettevõtja õigus. Tegevuskava ettevõtlusealase õiguskeskonna rahvusvahelise konkurentsivõime parandamiseks (Entrepreneurial Law. Action Plan for Improving the International Competitiveness of the Corporate Legal Environment). – *Juridica* 2006/4, p. 227 (in Estonian).

⁷⁷ S. Leibfried, C. Möllers, C. Schmid *et al.* Redefining the Traditional pillars of German Legal Studies and Setting the Stage for Contemporary Interdisciplinary Research. – *German Law Journal. Private Law* 2006 (07) 08, pp. 670–671. Available at http://www.germanlawjournal.com/pdf/Vol07No08/PDF_Vol_07_No_08_661-680_Articles_Leibfried.pdf (21.11.2008).

6. Conclusions

Following from the above, the author of this article takes the view that consideration should be given to the supplementation of Estonian law with provisions that would allow shareholders, who represent a certain proportion of share capital, to file a derivative claim on behalf of the company. The creation of such a threshold and procedure for the admissibility of proceedings, which would preclude litigation unreasonably burdening for the company, could be somewhat problematic. The hearing of the merits of the claim should certainly be preceded by a procedure by which the court first ascertains the admissibility of the claim. Although Estonian procedural law is not familiar with such a distinct type of procedure as an admissibility check, it does essentially exist *de lege lata*. For example, § 392 (4) of the Code of Civil Procedure^{*78} (CCP) does provide for verification of the correctness of acceptance of a matter and the prerequisites for permissibility of the action as a function of pre-trial proceedings. According to CCP § 371 (2) 1), the court may refuse to accept a statement of claim if, based on the facts presented as the cause of action, violation of the plaintiff's rights is not possible, presuming that the factual allegations of the plaintiff are correct, and also, according to subsection 2, if the action has not been filed for protecting the plaintiff's right or interest protected by law, or with an aim subject to legal protection by the state, or if such objective cannot be achieved by an action. The Explanatory Memorandum to the Code of Civil Procedure^{*79} also notes that the proceeding of a claim is essentially divided into verification of the admissibility of the action (decisions on refusal to accept or hear an action) and verification of the reasoning of the action (decision to grant or dismiss the action).^{*80}

Consideration should certainly be given to the question whether, if the possibility of derivative claims were introduced, it should necessarily become a minority right, and if so, what level of shareholding would allow for the application of such a remedy. It may be said that in addition to the legal possibilities directly provided by law, minority shareholders can form coalitions and exercise (various types of) activism through them, provided that they have sufficient common interest to do so. For example, in Sweden there have even been cases where the minority of a listed company acquires a majority with respect to the company as a whole via interest groups set up to pursue the common goals.^{*81}

In continental European public limited companies the concentration of holdings is considerably higher than in the USA and UK, where shareholdings are extremely fragmented.^{*82} The author of this article believes that if additional legal remedies were made available to minority shareholders, the peculiarities of Estonian public limited companies should certainly be taken into account. Entitling every shareholder of a listed company to file an action should not be our objective. The corporate governance of listed companies is generally subjected to more thorough rules, including as regards the legal position of shareholders (general meeting rules, distance voting, right to information, etc.).^{*83} The lack of shareholder control may even be a bigger problem in public limited companies that have few shareholders and that essentially stand between a private limited company and a listed company.

As a minimum, shareholders could be given the right to decide on the filing of claims not only against supervisory board, but also management board members, and to appoint representatives for such claims. In addition, shareholders representing 10% of share capital should also be entitled to derivative actions, because 10% is currently the general threshold for minority rights in Estonia.

The topic of developing an adequate company law framework also covers issues such as what position we wish to give shareholders in Estonian law and which legal rights should be protected, to what extent and by what means. It is certainly possible to strike a balance between the protection of minority shareholders' rights and the protection of companies from excessive interference by shareholders, while pursuing the goal of creating a secure investment environment. In any case, the objective of the legal regulation of directors' liability should be the stipulation of provisions that would ensure, under certain circumstances, the maximum possible likelihood of directors' liability.^{*84}

⁷⁸ Tsviilkohutmenetluse seadustik. Adopted on 20.04.2005. – RT I 2005, 39, 308; 2007, 16, 77 (in Estonian).

⁷⁹ Tsviilkohutmenetluse seadustiku eelnõu. Seletuskiri (Draft Code of Civil Procedure. Explanatory Memorandum). Adopted on 20.11.2003. Available at <http://web.riigikogu.ee/ems/saros-bin/mgetdoc?itemid=033370012&login=proov&password=&system=ems&server=ragne11> (in Estonian).

⁸⁰ Similarly, § 11 (3) 5) of the Code of Administrative Court Procedure (RT I 1999, 31, 425; 2007, 67, 413 (in Estonian)) allows the administrative court to return an action to the person who filed it and not hear the action if the person who filed the action or protest cannot obviously be entitled to refer to the administrative court, presuming that the person's factual allegations have been proved.

⁸¹ About shareholder activism, see A. Jansson. Collective Actions among Shareholder Activists. Thesis for the degree of Doctor of Philosophy. Växjö University. Sweden 2007.

⁸² C. van der Elst. Economic Analysis of Corporate Law in Europe: an Introduction. – Financial Law Institute Working Paper Series. WP 2002-01, p. 13. Available at <http://www.law.ugent.be/fli/WP/WP2002-pdf/WP2002-01.pdf> (21.11.2008).

⁸³ Certain issues are, e.g., covered by the Hea ühingujuhtimise tava (Good Corporate Governance Practice), 1.01.2006. Available at http://www.ecgi.org/codes/documents/cg_recommendations_2005_ee.pdf (21.11.2008) (in Estonian).

⁸⁴ F. A. Gewurtz (Note 47), p. 16.



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Subordination of Shareholder Loans in Estonian Law^{*1}

1. Introduction

One basis of a Continental European company are the capital rules whose purpose is the protection of creditors of companies and which prohibit the repayment of contributions to shareholders during the lifetime of a company. The concept of capital rests on the assumption that a company's assets are constituted by means of share capital, on account of which the creditors can satisfy claims submitted by them against the company.^{*2} Whether this objective can be achieved by means of capital rules is a different matter. It is clear that all business activities require a certain amount of capital. At the same time, the corresponding limits have not been established in Continental European law; the amount of obligatory investment has instead been determined by minimum capital requirements. In legislation, these requirements are established as universal for all companies and the company's actual capital needs are not taken into account.^{*3} If shareholders invest in a company in such a way that the share capital is constituted in a minimum amount prescribed by legislation and the rest of the capital needed for the company's activity is lent to the company, they have fulfilled their obligation to form share capital of a certain amount, but it is clear that the equity capital investment they made is not sufficient. In this way they do, however, create the possibility to take the investment from the company without having to undergo complicated procedures. It must also be taken into account that several Continental European countries either have already removed the minimum capital requirement from their legislation or plan to do this in the near future, which means that any formal equity capital investment requirement will cease to exist in these companies. In these conditions, the likelihood will further increase that all capital necessary will be given to the company as a loan.

It may also be inevitable that shareholders give loans to companies, because if a company is facing financial problems and needs additional capital to continue its activity, it is often in a situation in which acquiring additional capital from third parties (including banks) is impossible as all securable assets are already encumbered or third parties do not want to take excessive risks. In addition, capital from shareholders may be less expensive. In this case, there are also two possibilities: to make an equity capital investment (particularly by means of increasing share capital) and to give the company a loan.

The main difference between the forms of financing derives from bankruptcy rules. Although in both cases the investment is made by the same persons, their legal status is diametrically different — in order for a loan to be repaid, an ordinary claim can be submitted in bankruptcy proceedings, while returning equity capital can only be considered after the satisfaction of all claims submitted by creditors.

¹ This article was published with support from ESF Grant No. 6747.

² A. McGee, *Share Capital*. London 1999, p. 2.

³ By derogation, higher requirements apply in the financial services area, but these requirements depend on the type of activity and not on the extension.

A question arises as to whether such discretion can be complete. As giving a loan and making equity capital investment are financially equal investments from the point of view of the company and its creditors, merely providing this with a certain legal form should not be of determinative importance. While a shareholder is subject to the limited liability principle, the legal practice of each country also knows exemptions from this principle. Thus, there is no doubt that a claim for compensation of damages can be submitted against a shareholder who has been dishonest in his activities.

The issue regarding the legal status of loans given to a company by a shareholder primarily concerns whether such loans can be treated as regular loans or not. Here, problems may stem from different circumstances. At the same time, situations may arise wherein there are no negative objectives in giving a loan to the company in the form of an investment and the shareholders themselves agree that their claims are to be satisfied after the claims of all other creditors are satisfied. This choice, for instance, is justified in a situation in which a company needs a large investment for starting its activities, one that will no longer be needed after this. If the entire investment is made in equity capital in such a situation, it can only be returned by means of decreasing share capital, but this is an extremely long-term procedure accompanied by expenses. Considering that the duration of the procedure for decreasing capital exceeds six months according to the law, if the respective decision is made on the date of possibility of payment, the shareholders have to wait a very long time for their money, which is clearly economically ineffective because during this time the capital remains in the hands of the company, which no longer needs it.

The other problem regarding loans from shareholders is this: if we acknowledge the special status of shareholder loans, how is it possible to inform third parties thereof? As the corresponding publication is effected by means of the annual report, the central issue here is how these loans could and should be recorded in the balance sheet. It must be taken into account that false preparation of an annual report can be regarded as submission of incorrect information concerning the company's financial situation^{*4} under the Penal Code.^{*5}

2. The nature of a subordinated loan

A subordinated loan is usually defined as a loan that is subject to repayment upon termination of the debtor after the claims of all other creditors.^{*6} A subordinated loan is therefore a conditional claim of the lender against a company and the condition of repayment of debt is the prior satisfaction of claims of all other creditors of the company. On a regulatory basis, a loan can be subordinated by the law but in this case the legislation must include standards that prescribe the qualification of certain loans as subordinated loan. A loan may also be rendered subordinated by agreement, in which case one of the parties must be the provider of the loan. The other party to such an agreement is generally the recipient of the loan (the company), but it cannot be ruled out that a subordination agreement is concluded between the creditors and the company as a recipient of the loan does not enter this agreement.^{*7}

In the Continental European judicial area, the issue of subordinated loans is primarily treated under capital rules, which are based on two primary postulates: capital must be paid in and capital cannot be repaid.^{*8}

⁴ J. Sootak, P. Pikamäe. *Karistusseadustik: Kommenteeritud väljaanne* (Penal Code. Commented edition). 2nd supplemented and revised edition. Tallinn 2004. § 381 comment 3 (in Estonian).

⁵ *Karistusseadustik*. Adopted on 6.06.2001. – RT I 2001, 364, 2008; 13, 87 (in Estonian).

⁶ T. E. Stocks. *Corporate Finance: Law and Practice*. London 1995, p. 13.

⁷ For instance, the case law in the United Kingdom has acknowledged an agreement between the creditors in which the company did not participate as a subordination agreement. See E. Ferran. *Company Law and Corporate Finance*. London 1999, pp. 546–548.

⁸ J. Rickford. *Reforming Capital: Report of the Interdisciplinary Group on Capital Maintenance*. – *European Business Law Review* 2004 (15), p. 279.

3. The legal approach to shareholder loans in EU and other countries

3.1. The European Union

The Second Company Law Directive⁹, which regulates capital, includes provisions concerning distributions made to shareholders (in Article 15), but these rules concern only payment of interest to shareholders related to dividends and shares; they do not address other payments. In addition, the directive is only applicable to public limited liability companies and, although many Member States have also established similar requirements for private limited liability companies, it is not obligatory for these.¹⁰ In view of the extreme strictness of the directive in protecting capital, such an unfinished solution is further confirmation of the claim that, despite its strict requirements, the directive is in fact ineffective and does not regulate certain economically relevant issues that have repeatedly been pointed out by several authors.¹¹

The rules of European law regarding subordinated loans are included in banking directives, where they are handled in connection with prudential norms.¹² However, as the emphasis of these rules is different, there are also no rules regarding the possibility of subordinating loans. In addition, most companies fall outside the scope of application of these directives.¹³

3.2. Germany

In Germany, matters related to shareholder loans have been resolved differently at different times. First, the issue was dealt with in case law concerning limited liability companies. In these cases, by applying sections 30 and 31 of the *Gesetz betreffend die Gesellschaften mit Beschränkter Haftung* (GmbHG)¹⁴, the courts have considered loans to be subordinated loans when the loan was given to a company already experiencing solvency problems.¹⁵ The GmbHG in its § 30 lays down the prohibition of making payments to shareholders from assets that are necessary for preserving share capital, and § 31 sets forth the repayment obligation for payments made in violation of this prohibition. In 1984, the German Federal Supreme Court (BGH) extended these principles to public limited companies, though as a limitation stating that the shares of the shareholder providing the loan must account for more than 25% of the share capital.¹⁶ The courts relied on § 57 (on the contribution payment obligation of shareholders) and § 62 (on liability of shareholders in the case of illegitimate payments) of the *Aktiengesetz*¹⁷ (AktG).

In 1990, the matter of subordinated loans was regulated in Germany by means of legislation: § 32a and § 32b of the GmbHG, with the corresponding amendments made in 1994 to sections 39 and 135 of the *Insolvenzordnung*¹⁸ (InsO) and § 6 of the *Anfechtungsgesetz*¹⁹ (AnfG).

⁹ Second Council Directive of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (77/91/EEC). – OJ L 26, 31.01.1977, pp. 1–13.

¹⁰ In a report published in 1992, a proposal was made to extend the requirements of the directive to private limited-liability companies and a discussion was also held with regard to this proposal but no decision was made. See V. Edwards. *EC Company Law*. Oxford 1999, pp. 54–55.

¹¹ See, e.g., J. Armour. *Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law*. – *Modern Law Review* 2000 (63) 3, p. 355 ff.; L. Enriques, J. R. Macey. *Creditors versus Capital Formation: The Case Against the European Legal Capital Rules*. – *Cornell Law Review* 2001 (86) 6, pp. 1165 ff.; F. Kübler. *The Rules On Capital Under The Pressure Of The Securities Markets*. – K. J. Hopt, E. Wymeersch (eds.). *Capital Markets and Company Law*. Oxford 2003, p. 95 ff.

¹² Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions. – OJ L 177, 1-200; Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions. – OJ L 177, 201–255.

¹³ E. Werlauff has expressed the opinion that the provisions in these directives can be a source of inspiration for other public limited liability companies. The positive meaning of such inspiration remains unclear because as we are talking about prudential norms, voluntary application thereof may probably be considered, which any company would hardly undertake. See E. Werlauff. *EC Company Law. The common denominator for business undertakings in 12 states*. Copenhagen 1993, p. 145.

¹⁴ *Gesetz betreffend die Gesellschaften mit beschränkter Haftung* vom 20. April 1892. – RGBl. I p. 477.

¹⁵ A. Cahn. *Equitable Subordination of Shareholder Loans?* – *European Business Organization Law Review* 2006 (7), p. 289.

¹⁶ U. Huber, M. Habersack. *Special Rules for Shareholder Loans: Which Consequences Would Arise for Shareholder Loans if the System of Legal Capital Should be Abolished?* – *Legal Capital in Europe*. M. Lutter (ed.). Berlin 2006, p. 309.

¹⁷ *Aktiengesetz* vom 6. September 1965. – BGBl. I p. 1089.

¹⁸ *Insolvenzordnung* vom 5. Oktober 1994. – BGBl. I p. 2866.

¹⁹ *Gesetz über die Anfechtung von Rechtshandlungen eines Schuldners außerhalb des Insolvenzverfahrens* vom 5. Oktober 1994. – BGBl. I p. 2911.

In § 32a of the GmbHG, it is specified that if a shareholder has provided a company with a loan in a situation in which he could have increased the share capital as a diligent entrepreneur, he may claim the repayment of this loan in bankruptcy proceedings as a subordinated creditor. In addition, it has been laid down that if a loan has been obtained from third parties for the same reasons and a shareholder has secured the loan, the third party may submit a claim in the bankruptcy proceedings as a regular claim only to the extent that cannot be satisfied on account of securities. The conditions stated are also applied to other, economically equivalent transactions, and therefore the form in which the loan is provided is not important.^{*20}

In 1998, the legislation was once again amended in Germany and two exemptions were included in § 32a of the GmbHG. According to the first of these, the requirement to subordinate claims is not applied to shareholders not managing a company where the shareholder's holding is less than 10%. Under the second exception, those loans were cleared from subordination claims that had been given to the company by persons who had acquired a holding in the company during a crisis with the purpose of helping the company overcome solvency problems; this applies to all loans given by said persons.

Earlier case law and current legislation are at variance in certain ways in Germany. In § 30 of the GmbHG, which was applied to shareholder loans until the amendments in 1990 took effect, payments made to shareholders are limited in the extent corresponding to the deficit in equity capital, and § 32a prohibits repayment of a loan also if equity capital is not lost and as long as the company has not overcome the crisis. The other difference between § 30, which formed the basis for earlier judicial decisions, and § 32a, which currently regulates the matter, is that the latter is only applicable if the company is insolvent, while previous judicial decisions also considered it unlawful to repay the shareholder loans outside the context of bankruptcy proceedings.^{*21}

There is a plan to amend the legislation that is currently valid in Germany; the corresponding draft (MoMiG^{*22}) was published in 2006. According to the latter, the plan is to delete sections 32a and 32b of the GmbHG and supplement § 30 (1). The purpose of the proposed amendments is to simplify the rules and exclude payments made to shareholders in the interests of the company on the basis of an agreement from the restriction on making payments. In addition, some of the rules currently included under § 32a will be transferred to § 30 (1) (including the prohibition of repayment of a loan in the case where a shareholder has provided a loan where he could have made a contribution to the share capital as a decent operator). The amendments should primarily ensure that it is impossible to make payments to shareholders in a situation wherein equity capital has been lost, while carrying on regular economically justified transactions is not impeded (primarily cash pooling).

As has been noted, in Germany the provisions regarding subordinated loans are also in the bankruptcy law. The InsO's § 39, regulating the order of satisfaction of claims, ranks all loans provided by shareholders behind other creditors' claims; § 135 of the InsO prescribes the basis for recovery of repayment of shareholder loans; and § 6 of the AnfG lays down the same possibility in relation to reorganisation proceedings. These rules are in essence the same as those provided in the GmbHG.^{*23} If the special rules regarding subordinated loans otherwise apply to only the GmbH company form, the rules for bankruptcy proceedings apply to all companies.^{*24}

3.3. The United States of America

There are no provisions pertaining to shareholder loans in the United States of America, but there is a case law on subordination of loans. The US courts have made decisions related to the subordination of loans that are based on consideration of the fact that the managing shareholder has acted in a way that is unfair to the company. Such subordination may lack any connection with the loan itself or its repayment; instead, the basis for subordination (and the resulting ranking of the shareholder loan after the claims of the rest of the creditors) is merely the shareholder's dishonest behaviour. In application of this approach, the condition of the company at the time of receiving the loan from the shareholder is of no significance. It is also noteworthy that subordination of claims in the United States of America only occurs in bankruptcy proceedings.^{*25}

²⁰ A. Baumbach, A. Hueck. GmbH-Gesetz. 18., erweiterte und völlig überarbeitete Auflage. Leinen 2006, § 32a.

²¹ A. Cahn (Note 15), pp. 290–291.

²² Gesetzentwurf der Bundesregierung. Entwurf eines Gesetzes zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen (MoMiG). Stand 23. Mai 2007. Available at <http://www.bmj.bund.de/files/-/2109/RegE%20MoMiG.pdf> (19.11.2008).

²³ Münchener Kommentar zur Insolvenzordnung: InsO. 2. Aufl. Leinen 2008, § 135, margin number 8.

²⁴ U. Huber, M. Habersack (Note 16), p. 310.

²⁵ A. Cahn (Note 15), p. 292.

4. The legal approach to shareholder loans in Estonia

4.1. Subordination of loans by legislation

The first thing that must be said about the Estonian approach is that we lack company law provisions regarding subordination of shareholder loans. The first draft of the Commercial Code^{*26} included a provision corresponding to § 32a of the GmbHG with regard to private limited companies, but it was deleted from the draft. The Bankruptcy Act^{*27} does not discuss the matter of subordinated loans. Estonia also lacks case law in the corresponding field. It is therefore impossible to describe the existing situation, but a question must be raised as to whether current legislation allows subordination of shareholder loans.

The term 'subordinated loan' is not unknown to Estonian legislation; it has been used in acts regulating providers of financial services (credit institutions^{*28}, insurance undertakings^{*29}, electronic money institutions^{*30}, investment firms^{*31}, and fund management companies^{*32}). However, these acts do not address subordinated loans from the company law standpoint; instead, subordinated loans have been regulated as a part of equity capital and an order has been established by the respective legal provisions, according to which loans taken out by companies in the financial services sector that correspond to certain conditions can be treated as equity capital. There is also the difference here that subordinated loans are not equal to shareholder loans; they can also be provided by third parties. Provisions relevant to company law are included in the Credit Institutions Act only because it states that a subordinated claim is subject to repayment after satisfaction of the claims of the rest of the creditors (§ 131 (2)). Although all of the acts mentioned overlap, regulating essentially the same matter, others lack corresponding provisions for other sectors, and cases in these areas are thus subject to general rules (or lack of rules, to be more exact).

In connection with the absence of direct provisions in current Estonian legislation, our situation is in many respects similar to that seen in Germany before 1990. Payments to shareholders of a private limited company are regulated by § 157 (1) of Commercial Code, which specifies that dividends to shareholders may be taken from net profit or retained earnings from previous financial years, from which the non-covered loss of previous years has been deducted. Paragraph 3 of the same section prohibits payments to shareholders if the company's net assets recorded in the annual report approved by the company at the end of the previous financial year are less or would be less than the total amount of share capital and reserves specified as the upper limit for payment to shareholders in relevant legislation or the articles of association. Payments to shareholders of public limited companies are regulated by § 275 (1) of the Commercial Code, which prohibits the repayment of a contribution to a shareholder (this is essentially the same provision as § 57 (1) of the AktG); § 276 (1), which links the permissibility of making payments with the end of the financial year; and sentence 3 of § 278, which defines the maximum amount of dividends that may be paid to shareholders (based on Article 15 of the Second Company Law Directive). It is noteworthy that, although the norms regarding a private limited company and a public limited company have mostly been harmonised and the capital rules also should be the same for these two cases, the text of the act is slightly different with respect to these as a result of the use of different sources.

The first issue related to the given norms is whether the same situation has been handled differently for a private limited company and a public limited company. The text of the act itself is practically the same, and it therefore seems groundless to seek two different situations. When considering the decisions of shareholders, the Supreme Court has found that there is no justification for treating the same situation differently in a private limited company and a public limited company.^{*33} Although we must agree with this view of the Supreme Court on the basis of the case considered and the same viewpoint should be justified currently as well, it must be noted that the Supreme Court filled a gap in the legislation while in the case of the legislation currently in effect, there are legal provisions and the matter can be interpreted pursuant to these. At the same time, there is no basis for interpreting the provisions differently.

²⁶ Äriseadustik. Adopted on 15.02.1995. – RT I 1995, 26/28, 355; 2008, 16, 116 (in Estonian).

²⁷ Pankrotiseadus. Adopted on 22.01.2003. – RT I 2003, 95; 2007, 67, 413 (in Estonian).

²⁸ Krediidiasutuste seadus (Credit Institutions Act), § 741. Adopted on 9.02.1999. – RT I 1999, 23, 349; 2008, 3, 21 (in Estonian).

²⁹ Kindlustustegevuse seadus (Insurance Activities Act), § 68. Adopted on 8.12.2004. – RT I 2004, 90, 616; 2007, 68, 421 (in Estonian).

³⁰ E-raha asutuste seadus (Electronic Money Institutions Act), § 37. Adopted on 19.10.2005. – RT I 2005, 61, 473; 2007, 65, 405 (in Estonian).

³¹ Väärtpaberituruseadus (Securities Market Act), § 97. Adopted on 17.10.2001. – RT I 2001, 89, 532; 2008, 13, 89 (in Estonian).

³² Investeeringimisfondide seadus (Investment Funds Act), § 86. Adopted on 14.04.2004. – RT I 2004, 36, 251; 2008, 13, 89 (in Estonian).

³³ CCSCd 3-2-1-6-03, 29 January 2003. – RT III 2003, 4, 41 (in Estonian).

It must also be emphasised that the provisions regarding making of payments were initially different in their text but, with the inclusion of a provision in § 278 of the Commercial Code corresponding to Article 15 of the Second Company Law Directive³⁴ and the simultaneous amendment of § 157 of the Commercial Code, the differences were eliminated. Therefore, it can be said that the most direct source of the norm related to a private limited company as well as a public limited company is the directive and that, in view of the purpose of the directive alone, this is simply a provision regulating dividend rates.

The next issue is the content and purpose of the provisions. Here, it must first be noted that the section headings are confusing. The heading of § 278 of the Commercial Code, regarding a public limited company, is 'Amount of dividend', which should confirm that this provision is to be applied to dividend payments only. A similar provision concerning private limited companies is § 157 (3) of the Commercial Code, the heading of which is 'Making of distributions'. At the same time, however, the heading of a section has no meaning as such. It does not include a legal provision, and one cannot proceed from the heading in determining the content of the provision; therefore, the failed headings should not have an impact on the interpretation and application of the provision. The confusion with the headings probably stems from the fact that § 157 of the Commercial Code initially also included a subordination rule corresponding to § 32a of the GmbHG, which is the reason the scope of application of the provision was wider, and after its removal from the draft the section heading remained the same and thereby became inaccurate.

The above arguments support the viewpoint that the corresponding provisions of the Commercial Code do not allow the treatment of shareholder loans as subordinated loans. However, such a conclusion cannot be justified. It must first be noted that the provisions discussed do not speak of dividends but, instead, prohibit the shareholders from making payments in certain situations, which provides the possibility to regard other payments in addition to dividends as such payments. Another issue is the purpose of the provision, which is to prohibit making payments to shareholders in excess of share capital — in essence, making payments on account of external finances. Such an objective cannot be limited by a formal dividend payment alone but must extend to all cases because otherwise the principle that shareholders receive from the company what they have provided only if the claims of the creditors are satisfied is infringed. The opposite interpretation would be contrary to the principle of good faith. In addition, the fact cannot be overlooked that Estonian case law often proceeds from principles that have been accepted in Germany, and, considering the legal practice of the latter, our courts can also proceed from the same goals even if the standards are different. From a legal political perspective, such an approach in the given case may even be justified, because otherwise a situation could arise with respect to the free movement of capital in which investors discover Estonia as a country where one can create a better situation for oneself when compared to other countries, whereby the purpose of such an advantage would not be *bona fide*.

4.2. Loan subordination agreements

Subordination of a loan by agreement occurs when a creditor of a company agrees that his loan will be returned after the claims of all other creditors are satisfied.³⁵ As such agreements are not directly regulated by legislation, a corresponding agreement is subject to the general legal rules, including the principle of freedom to determine the content of a contract. The latter gives rise to the question of whether such agreements are allowed. As there are no common and clear rules regarding the given cases in Estonia, there are also no clear prohibitions. However, it cannot be said that there are no restrictions, as these may arise from the nature of some provisions. We can only agree that such assessments are also generally the most complicated in nature³⁶, and the given case is further complicated by the fact that the existence of limitations may arise not from the standards of private law but from those of procedural law.

As the subordination of a loan determines the ranking of its repayment in relation to others, the issue regarding freedom of contract is also primarily related to the general order of satisfaction of claims. This matter is regulated by § 153 of the Bankruptcy Act, which determines the order of satisfaction of claims. This also gives rise to the question of whether the Bankruptcy Act represents imperative rules or it is also possible to agree differently from what it sets forth. A position should definitely be taken that the order of satisfaction of claims cannot be amended such that creditors agree among themselves on some seemingly random order. One of the purposes of a bankruptcy proceeding is clarity of the proceedings, and in this case this principle would be infringed. At the same time, a subordinated loan may be considered to be one exemption, the nature of which gives rise to the need to apply special rules — i.e., placing the claim in a ranking that is not prescribed by the Bankruptcy Act.

³⁴ In essence, the text of the directive was transposed word for word and a different solution would have probably been impossible considering the normative nature of the directive. See C. Villiers. *European Company Law — Towards Democracy?* Aldershot 1998, pp. 28–29.

³⁵ See E. Ferran (Note 7), p. 549.

³⁶ Võlaõigusseadus I. Üldosa (§§ 1–207): Kommenteeritud väljaanne (Law of Obligations Act I. General Part (§§ 1–207): commented edition). P. Varul, I. Kull, V. Kõve, M. Käerdi (eds.). Tallinn 2006, § 5 comment 4.4.4 (in Estonian).

A solution to this problem may be sought in case law; however, this is extremely poor. We know of only one case in which the issue of subordinated claims has been disputed.^{*37} In that case, a bank had received a loan by means of two different agreements, for a loan conditionally subject to repayment and a subordinated loan. In making its decision, the Supreme Court treated these loans as subordinated loans and agreed with the lower courts, which had decided that the claims made were to be subject to satisfaction after claims that were not submitted in due time but are qualified. Here, the Supreme Court applied § 37 (2) 4) of the Credit Institutions Act^{*38} valid until 30 June 1999, which laid down the definition of a subordinated loan. It is noteworthy that in the legislation applied here, there were no standards regarding the way in which claims arising from subordinated loans should be satisfied in a bankruptcy proceeding and the court regarded the loan as subordinated on grounds that the claim arising from the subordinated loan was included under the credit institution's own funds according to § 37 (2) 4) of the Credit Institutions Act. Therefore, according to the court's conclusions, ranking of these loans was a result of an agreement between the parties. The court has not based its decision on any other arguments, nor has it provided any broader treatment of subordinated loans.

We must agree with the position of the Supreme Court with regard to the agreement between the parties and the resulting subordination of the loan. It is noteworthy that the Supreme Court gave preference to an agreement between the parties over the legislation, which did not include special rules regarding subordinated loans. In general, this means that the Supreme Court is of the opinion that by agreement parties can establish a claims arrangement different from the one prescribed by the Bankruptcy Act for the ranking for satisfying claims, at least insofar as the creditor's claim is ranked lower by agreement than is prescribed by legislation (the court has not said anything with regard to the reverse situation, which it is unlikely could be allowed). That § 86 of the Bankruptcy Act^{*39} as applied, which was valid until 1 January 2004 and is currently invalid, did not prescribe a ranking in which the court was to place the disputed claims implies that the list of rankings prescribed by legislation is not exhaustive and it should therefore also be allowed to supplement this by means of an agreement. Here a reservation must probably be made that such an amendment could concern a change in rankings backward but not forward.^{*40} It may therefore be concluded from the views of the Supreme Court that the subordination of loans by agreement is possible and allowed.

Unfortunately, the decision of the Supreme Court referred to here includes relatively few arguments. It is also impossible to determine all of the circumstances of the case, which makes it problematic to rely on this solution. Among other things, there are no indications as to the viewpoints of the parties, which may be of determinative importance. It is thus impossible to determine whether the plaintiff in this case relied on the argument that it is impossible to change the order for the satisfaction of claims prescribed by legislation by agreement. If he did not rely on this argument, it cannot be said that the Supreme Court has assessed amendment of the order for the satisfaction of claims by agreement. As to the case of a contractual subordination of claims, it must also be pointed out that, in connection with the latter, it is not quite accurate to speak about shareholder loans, as any creditor may subordinate his claim in this manner. Problems of a different nature may arise here if the corresponding claim is secured by a pledge, as this inevitably gives rise to the question of whether to regard these claims as claims secured by a pledge or as subordinated claims.

5. Conclusions

It is probably impossible to provide uniform answers to the questions raised in the introduction to this paper. If we take only the above-mentioned German or US approach to the issue of subordinated loans as an example, fundamental differences can be seen, which point to the question of whether results achieved with different methods are fundamentally different. All in all, the objective of avoiding unfair situations in both countries is the same. Therefore, the issue of the methods implemented is not primary in some sense.

On the other hand, current legislation regarding subordinated loans in Estonia is more similar to the legislation in the United States of America — both lack standards regarding the problem considered here. It should be kept in mind here that judicial precedent in these legal orders has a different meaning and that the options of a court are also different and, thus, the lack of rules in Estonian legislation must be considered abnormal. Therefore, regardless of the solution, I dare to claim that the establishment of any rules is better than the current disorder.

The answer to the question of whether loans given to a company by shareholders should be treated differently from all other loans is affirmative. It is not justified to grant the investments that shareholders have made

³⁷ CCSCd 3-2-1-114-00, 17 January 2001. – RT III, 2001, 3, 30.

³⁸ Krediidiasutuste seadus. Adopted on 15.12.1994. – RT I 1995, 4, 36; 1999, 23, 349 (in Estonian).

³⁹ Pankrotiseadus. Adopted on 10.06.92. – RT I 1992, 31, 403, 2003; 17, 95 (in Estonian).

⁴⁰ For instance, the case law of United Kingdom allows the amendment of the *pari passu* principle precisely in this manner. See E. Ferran (Note 7), pp. 550–552.

in the company as a loan or as a contribution to equity capital a diametrically different legal status, as it is accompanied by potential abuses and may give unjustified advantages to shareholders in circumstances wherein they are in control of the company's management. It may also make it too easy to ensure low risk of the loss of the investment; given the limited responsibility of these persons for the company's liabilities, the risk is already relatively small. Therefore, the subordination of loans is justified and the inclusion of corresponding rules in our legislation merits serious consideration. At the same time, a stance should be taken that existing standards can also be relevantly applied.

The other issue examined in this paper was whether loan subordination agreements are allowed. At a fundamental level, there is nothing wrong with such agreements and current legislation also lacks rules prohibiting them. Therefore, loan subordination agreements must be regarded as valid. The status of such agreements is indeterminate in bankruptcy proceedings, but, if one proceeds from the point of view of the Supreme Court, claims resulting from these agreements must be given a ranking that in essence corresponds to the content of the claims (i.e., after the claims of all other creditors).

In conclusion, it must be noted that, by means of the Second Company Law Directive, the EU has tried to establish common standards among its member states with regard to capital rules. What is stated in the present article should provide grounds for the claim that no unity can actually be spoken of. We can conclude from this, in turn, that the regulatory framework established by the second directive must be replaced with rules proceeding from the goal.



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Implications of the Smallness of an Economy for Merger Remedies

There has been increasing discussion in recent years concerning the particularities of small economies in the context of competition law and policy.^{*1} It has been generally recognised that market structures in small economies tend to be more concentrated than market structures in large economies, where economies of scale and scope are important. There have been voices arguing that such features may call for specifically tailored competition rules.^{*2}

This article studies the implications related to the small size of an economy for merger control and, in particular, remedies applicable in merger control. The article questions whether the principles applicable to the use of merger remedies in large economies are equally appropriate in small economies.

In order to seek an answer to this question, section 1 of this article first discusses in brief the effects of the smallness of an economy on competition, pointing to some factors that tend to cause distinct outcomes in small economies, such as high concentration rates and entry barriers. Section 2 of this article deals with remedies applicable in the case of anti-competitive (illegal) mergers, first giving a brief overview of some procedural considerations related to merger remedies, the different types of remedies applicable in merger control, and the principles for the choice of remedies in various competition regimes. Thereafter, it discusses the justification for wider use of behavioural remedies in small economies, as compared to large economies, coupled with various case studies. Finally, some conclusions follow.

It should be noted at the outset that, even though there are various ways to define smallness of an economy, for the purposes of this article economies whose population is below 10 million are considered small. Setting of any such dividing line is a rough decision, and as the threshold for smallness is moved up or down, the weight of the various arguments concerning the particularities of small economies changes — the specific

¹ OECD Global Forum on Competition. *Small Economies and Competition Policy: A Background Paper*. – CCNM/GF/COMP(2003)4, February 2003. Available at <http://www.oecd.org/dataoecd/57/57/2486546.pdf> (30.07.2008) (hereinafter: OECD Background Paper); M. Gal. *Size Does Matter: The Effect of Market Size in Optimal Competition Policy*. – *Southern California Law Review*, September 2001, pp. 1437–1478; L. Evans, P. Hughes. *Competition Policy in Small Distant Open Economies: Some Lessons from the Economics Literature*. – New Zealand Treasury Working Paper 03/31, December 2003. Available at <http://www.treasury.govt.nz/publications/research-policy/wp/2003/03-31/twp03-31.pdf> (30.07.2008); H. Horn, J. Stennek. *The Political Economy of EU Merger Control: Small vs. Large Member States*. 21.09.2005. Available at <http://www.econ-law.se/Papers/Horn-Stennek-revised.pdf> (30.07.2008); Competition, Regulation and Development Research Forum (CDRF). *Competition and Regulatory Regimes in Small & Developing Countries*. – Policy Brief 2/07. Available at <http://www.circ.in/pdf/PolicyBrief2.pdf> (30.07.2008); Competition Law Forum. *Small Economies and Competition Policy — A Fair Deal? Summary of conference presentations and discussions*. Luxembourg, October 2007. Available at http://www.eventsforce.net/OXYGEN/media/uploaded/EVOXYGEN/event_82/Small%20Economies%20Conference%20-%20Summary%20transcript.pdf?popup=1 (30.07.2008).

² *Ibid.*

features associated with smallness grow progressively more apparent the smaller the nation and less apparent the closer the size of the nation is to the threshold.

1. Effects of smallness on competition

One of the most widely recognised effects of smallness of an economy is the difficulty of achieving minimum efficient scale (MES) for domestic firms, on account of low domestic demand. As Michal S. Gal has put it, “[t]he basic handicap resulting from small size is the need to produce at levels that cater to a large portion of demand in order to achieve minimum costs of production”.³ Therefore, small economies can support only a small number of competitors in many industries, which is why their markets tend to be highly concentrated.⁴

In many cases, the problem of smallness of domestic markets can be mitigated by opening the markets to trade — foreign markets can broaden the sources of demand and increase the potential for actualising the expansion that is necessary for achieving MES, by exploiting economies of scale and scope. At the same time, imports can supplement or replace lacking domestic production. This means that where domestic production is too costly or impossible because of the problem of achieving MES or on account of scarcity or lack of resources, import goods could satisfy the demand in small economies.⁵

The benefits of trade have been recognised around the world, and, with respect to many goods; this has greatly alleviated the problems of achieving MES domestically and has opened up many domestic markets to competition from foreign firms as well. As a result, the majority of markets in small, open economies are composed, solely or to a great extent, of imported products; and the number of markets that are solely or mostly supplied by domestic products is rather limited.⁶

However, even in the case of the most liberal trade regulations, barriers to trade may still exist. Therefore, an economy’s openness to trade cannot fully resolve the problems related to small size in every industry. This is because of the existence of irremovable barriers to trade, such as natural barriers (e.g., oceans, mountains, and large distances), cultural or language differences, consumer preferences, and high transportation costs.⁷ The effect of such factors on trade depends greatly on the nature of the goods or services.⁸ For instance, perishable goods (such as fresh milk products and fresh bakery products) that have a short storage life can be traded only within limited distances. Similarly, trade is unlikely where the value-to-weight or value-to-size ratio of the goods in question would render transportation irrational on account of high costs.⁹ Other factors, such as consumer preferences, culture, and language differences can complicate trade as a consequence of the need to customise the goods for the target market or of the need to break the established brand loyalty with respect to domestic products.¹⁰

Such obstacles to trade are likely to cause proportionally more significant segmentation in certain economies than in others. The more distant the economy is from its potential trade partners either naturally or culturally, the higher are the barriers to trade and the larger is the number of non-tradable sectors. Furthermore, an economy being of small size may discourage trade, because the investment costs of adapting to local consumer preferences or language requirements are proportionately higher as compared to those in large economies. Therefore, small and/or distant economies will always be more prone to face problems of achieving MES, particularly with respect to non-tradable goods and those goods that face significant trade barriers.

Furthermore, smallness of an economy could constitute a factor raising entry barriers for potential market participants. Since the demand in small markets is limited, certain kinds of entry barriers, such as lack of economies of scale and scope, are likely to be harder to overcome in small economies than in large ones. This is because an entrant with plants of less than MES would face cost disadvantages *vis-à-vis* firms with MES plants. It has been reasoned that if MES is large relative to demand and if the cost penalties for operating below MES are substantial, a new firm would have to enter the market at such a large scale that the combined output of all firms operating in the market could be sold only at substantially reduced prices, perhaps even below average

³ M. Gal (Note 1), pp. 1439–1441.

⁴ See, e.g., M. Gal. Competition Policy in Small Economies — Prepared Remarks for the OECD Session on Small Economies. — CCNM/GF/COMP/WD(2003)42, February 2003. Available at <http://www.oecd.org/dataoecd/57/28/2486919.pdf> (30.07.2008); H. Horn, J. Stennek (Note 1); Competition law forum (Note 1); OECD Background Paper (Note 1).

⁵ OECD Global Forum on Competition. Estonia — Competition Problems in a Small Country. — CCNM/GF/COMP/WD(2003)5, January 2003. Available at <http://www.oecd.org/dataoecd/57/44/2486151.pdf> (30.07.2008).

⁶ *Ibid.*

⁷ M. Monti. Market Definition as Cornerstone of EC Competition Policy. Speech/01/439, Workshop on Market Definition, Helsinki Fair Centre, October 2001. Available at <http://ec.europa.eu/comm/competition/speeches/> (30.07.2008).

⁸ H. Horn, J. Stennek (Note 1), pp. 7–9.

⁹ *Ibid.*

¹⁰ M. Monti (Note 7).

total cost, unless one of the firms exits the market.^{*11} Moreover, a small market can be unattractive also simply because of the maximum potential total return on investment being smaller than that in large markets.

Small size may also create more competition problems if the existing competitors control concentrated, vertically-linked markets. In particular, the existence of high MES levels in one market might limit entry into a vertically-linked market if it requires a new entrant to enter more than one market in the chain of manufacturing and distribution, or if it significantly raises that entrant's costs relative to the costs of its rivals.^{*12} Such impediment can be both structural and strategic in nature.^{*13}

With MES considerations left to the side, limited human resources can also constitute an entry barrier, since small population size often constrains the availability of human capital, especially skilled labour. Furthermore, most small economies are also small in geographic terms, which tends to entail a limited and less diversified supply of natural, irreproducible resources.^{*14}

Such problems are exacerbated to the extent that domestic regulations inhibit rather than enhance competition. For example, the existence of country-specific distribution regulations could constrain market entry. Thus, it is of particular importance for small economies to ensure the openness of distribution systems and not maintain regulations favouring the existing market participants.^{*15} In sectors where competition is severely limited, regulation targeted at loosening the ties present between various existing market participants may be needed to limit the potential costs imposed by the presence of market power.^{*16} As will be seen below, in the case of mergers that are potentially anti-competitive, remedies can be applied for such regulation.

2. Remedies in the case of anti-competitive mergers

2.1. Overview of some procedural considerations related to merger remedies

Whenever a merger would have serious anti-competitive effects, it is usually deemed illegal in all jurisdictions where merger control is in force. Depending on the procedural arrangements (either a pre-merger notification system or post-merger assessment), the competition authority investigating such a merger is tasked with prohibiting the merger or declaring its illegality in order to avoid detriment to competition.^{*17}

Alternatively, most jurisdictions allow modifications to be made in the merger arrangements in order to remove or at least mitigate the competition concerns raised by the merger; i.e., remedies are applied. Such modifications constitute commitments by the merging parties to fulfil certain obligations or achieve certain outcomes, such as to divest some assets or businesses, or to act in a specified manner. The competition authority's approval of the merger could be made conditional on compliance with such requirements, or a fine could be specified for the case of non-compliance.^{*18}

The aim of the remedies is to avoid prohibiting the merger transaction as a whole while at the same time remedying the loss of free competition and diminishing the potential harm to competition. As it is in the interests of the merging parties to avoid the prohibition of their contemplated merger, it is usually up to them to propose adequate modifications. Depending on the procedural rules, such modifications can be made as amendments to the merger notification submitted by the merging parties, as additional proposals by the merging parties, or as a result of negotiations between the merging parties and the competition authority.^{*19}

¹¹ M. Gal (Note 1), p. 1445.

¹² *Ibid.*, p. 1448.

¹³ See more on the distinction of structural and strategic trade barriers from OECD Policy Brief. Competition and Barriers to Entry. January 2007. Available at <http://www.oecd.org/dataoecd/9/59/37921908.pdf> (30.07.2008).

¹⁴ *Ibid.*, p. 1447.

¹⁵ OECD Global Forum on Competition. Denmark — Special Aspects of Competition Policy in Small Economies. – CCNM/GF/COMP/WD(2003)16, January 2003, p. 2. Available at <http://www.oecd.org/dataoecd/58/26/2485941.pdf> (30.07.2008); OECD Global Forum on Competition. Ireland — Special Aspects of Competition Policy in Small Economies. – CCNM/GF/COMP/WD(2003)18, January 2003, p. 4. Available at <http://www.oecd.org/dataoecd/58/8/2485758.pdf> (30.07.2008); OECD Global Forum on Competition. Malta — Competition Policy in Small Economies. – CCNM/GF/COMP/WD(2003)32, January 2003, p. 7. Available at <http://www.oecd.org/dataoecd/57/8/2486833.pdf> (30.07.2008); OECD Global Forum on Competition. Switzerland — Special Aspects of Competition Policy in Small Economies. – CCNM/GF/COMP/WD(2003)18, January 2003, p. 4. Available at <http://www.oecd.org/dataoecd/58/22/2486055.pdf> (30.07.2008).

¹⁶ OECD Global Forum on Competition. New Zealand — Competition Policy in Small Economies: Issues Arising. – CCNM/GF/COMP/WD(2003)29, January 2003, p. 7. Available at <http://www.oecd.org/dataoecd/57/53/2486698.pdf> (30.07.2008).

¹⁷ Author's conclusion on the basis of the data available in The Global Merger Control Manual. 7th edition. D. J. Laing, L. A. Gomez (eds.). Cameron May, 2007.

¹⁸ *Ibid.*

¹⁹ *Ibid.*

Where the enforcement of remedies imposed in a merger authorisation requires monitoring, independent trustees or experts are sometimes used in some jurisdictions to oversee the parties' compliance with the obligations imposed. The costs of hiring the trustees are normally borne by the parties, as it is in the parties' best interests, in order to avoid prohibition of the merger, to provide the competition authority with sufficient assurance that the commitments are going to be complied with and to minimise the competition authority's monitoring costs.^{*20}

2.2. Types of remedies

Remedies are typically classified into two broad categories — structural and behavioural. Structural remedies are those that are designed to make changes to the structure of the market, whereas behavioural remedies regulate the conduct of the merging parties after the merger.

The most typical structural remedy is divestiture of a business, a set of assets, or productive capacity. The aim of such a remedy is to create or strengthen a source of competition to the merged entity in order to restore or maintain competition in the relevant market after the merger. In addition to divestiture, long-term and exclusive licensing of intellectual property rights and removal of links with competitors are considered structural.

Other remedies are typically considered behavioural. Such remedies may be targeted to deal with varying competition concerns. Firstly, there are measures aimed at facilitating horizontal rivalry. Such remedies may be designed to

- (i) prevent the merged entity from using its horizontal market position to foreclose the market and lessen competition (e.g., commitments not to engage in tying, predatory pricing, or exclusive and long-term agreements);
- (ii) prevent the merged entity from using its vertical integration to distort or limit horizontal rivalry (e.g., commitments to grant access to key infrastructure on regulated price and other terms); and
- (iii) change buyers' behaviour in order to encourage competition (e.g., commitments to provide information to buyers and facilitate the process of switching providers).^{*21}

Secondly, there are measures aimed at preventing exploitative behaviour on the part of the merged entity after the merger by controlling its outcomes. Such remedies include price caps, service level agreements, and supply or purchase commitments.^{*22}

Some of the behavioural remedies may entail some structural effect on the market (e.g., granting access to infrastructure), while others are purely behavioural and may not in fact amount to more than a promise not to abuse market power. Often packages including different types of remedies are used. For instance, behavioural remedies may be necessary to supplement structural remedies in the interim between the adoption of the decision to authorise the merger and the completion of the divestiture. Similarly, there might be a package of various behavioural remedies.

As is apparent from the discussion above, the range of remedies is rather wide. However, legal rules and principles of individual legal systems, as well as declared enforcement policies, may pose conditions and limits as to the range of remedies available to the merging parties in a particular competition regime. An overview of such considerations is given below.

2.3. Principles of the choice of remedies in various competition regimes

Both the US and the EU merger control systems have clearly declared a preference for structural remedies. It is stated in the US Department of Justice Antitrust Division's 'Policy Guide to Merger Remedies' that "[s]tructural remedies are preferred to conduct remedies in merger cases because they are relatively clean and certain, and generally avoid costly government entanglement in the market".^{*23}

²⁰ See, e.g., ICN Merger Working Group, Analytical Framework Subgroup. Merger Remedies Review Project – Report for the 4th ICN annual conference, Bonn, June 2005, pp. 14–15. Available at http://www.internationalcompetitionnetwork.org/media/library/conference_4th_bonn_2005/Remedies_Study.pdf (30.07.2008).

²¹ *Ibid.*, pp. 11–12 and 17–18.

²² *Ibid.*, pp. 12 and 18–19.

²³ US Department of Justice (DOJ) Antitrust Division. Policy Guide to Merger Remedies, October 2004, section 3.A. Available at <http://www.usdoj.gov/atr/public/guidelines/205108.htm> (30.07.2008). Similarly, the Statement of the Federal Trade Commission's Bureau of Competition on Negotiating Merger Remedies, 2 April 2003 (available at <http://www.ftc.gov/bc/bestpractices/bestpractices030401.shtml> (30.07.2008)) sets forth a similar principle.

In the EU, the European Commission's draft notice on remedies indicates that "commitments which are structural in nature, such as the commitment to sell a business unit, are, as a rule, preferable from the point of view of the [Merger Regulation], inasmuch as such commitments prevent, durably, the competition problem which the Commission considers would be caused by the merger as notified, and do not, moreover, require medium or long-term monitoring measures. Nevertheless, the possibility cannot automatically be ruled out that other types of commitments may also be capable of preventing the significant impediment of effective competition."²⁴ The European Commission has stated its willingness to accept remedies that do not amount to more than purely behavioural promises only in exceptional circumstances, such as in respect of competition concerns arising in conglomerate structures.²⁵

Structural remedies are generally considered preferable also in the German²⁶ and UK²⁷ merger control systems.

Similarly to large merger control systems, various smaller systems give preference to structural remedies. For example, in New Zealand the Commerce Commission can only accept structural commitments to divest assets or shares and cannot accept behavioural commitments.²⁸ In Slovenia, the standards for remedies are such that, even though behavioural remedies are not expressly excluded, they are unacceptable in practice.²⁹ The working group set up by the Nordic competition authorities (including those of Finland, Sweden, Denmark, and Norway) has also expressed a preference for structural remedies.³⁰ However, as will be seen from case studies presented below, they are still willing to adopt a flexible view toward behavioural remedies.

Conversely, there are several small economies wherein behavioural remedies are considered to be the preferred remedy. For instance, according to J. Amols, senior desk officer of the Latvian Competition Council, even though both structural and behavioural remedies are acceptable, the council considers purely behavioural remedies the most effective type of remedies, because remedies of this kind are less burdensome for merging parties and are also easier to control from the side of the council.³¹ Similarly, P. Gorecki, the director of the Mergers Division of the Irish Competition Authority, has expressed that "if there is a choice between a behavioural and a structural remedy the former is preferred".³² Behavioural remedies have so far played the primary role also in the merger control practice of Austria³³, the Czech Republic³⁴, Greece³⁵, and Serbia.³⁶ Below, a few examples of cases wherein behavioural commitments have been used in some of these jurisdictions are described.

²⁴ Commission Notice on Remedies Acceptable under Council Regulation (EEC) No. 139/2004 and under Commission Regulation (EC) No. 802/2004 (draft), section 15. Available at http://ec.europa.eu/comm/competition/mergers/legislation/draft_remedies_notice.pdf (30.07.2008) (hereinafter: Commission's draft notice on remedies). Similar principles are declared in the currently valid Commission Notice on remedies acceptable under Council Regulation (EEC) No. 4064/89 and under Commission Regulation (EC) No. 447/98, section 9. Available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2001:068:0003:0011:EN:PDF> (30.07.2008).

²⁵ Commission's draft notice on remedies, section 69.

²⁶ Section 40 (3) of the German Act against Restraints of Competition (available at http://www.bundeskartellamt.de/wEnglisch/download/pdf/06_GWB_7__Novelle_e.pdf (30.07.2008)) clearly prohibits the imposition of remedies requiring continued monitoring.

See also H. Bergmann, F. Röhling, Germany, in *Getting the Deal Through: Merger Control 2008*, question 22. Available at http://www.gettingthedealthrough.com/crossborder.php?region_id=16§or_id=71 (30.07.2008).

²⁷ UK Competition Commission. Merger References: Competition Commission Guidelines, June 2003, paragraph 4.15. Available at http://www.competition-commission.org.uk/rep_pub/rules_and_guide/pdf/cc2.pdf (30.07.2008).

²⁸ A. Peterson, S. Keene. New Zealand, in *Getting the Deal Through: Merger Control 2008*, question 22. Available at http://www.gettingthedealthrough.com/crossborder.php?region_id=16§or_id=71 (30.07.2008).

²⁹ Judgment of Administrative Court of Republic of Slovenia, Case No. U 1286/2003 of 18 June 2004 in *Interbrew Central European Holding B.V., Pivovarna Laško d.d. and Pivovarna Union d.d. v. Competition Protection Office*, cited through P. Pensa. Slovenia — Merger Control. — Competition Cases from the European Union. I. Kokkoris (ed.). London: Sweet & Maxwell 2008, pp. 1141–1152, paragraphs 25–042 and 25–051.

³⁰ Nordic Working Group. Commitments Concerning Concentrations between Undertakings, Summary of a Report from a Nordic Working Group 2003. Available at http://www.kkv.se/upload/Filer/ENG/Publications/koncentration_utsidan.pdf (30.07.2008).

³¹ E-mail of J. Amols, Senior Desk Officer of the Latvian Competition Council, to the author, dated 29.02.2008.

³² E-mail of K. MacGuill, Economist of the Irish Competition Authority to the author, dated 14.03.2008, forwarding the views of P. Gorecki.

³³ C. Vartian. Austria — Merger Control. — Competition Cases from the European Union. I. Kokkoris (ed.). London: Sweet & Maxwell 2008, paragraph 2-078. See also A. Reidlinger, A. Zellhofer. Austria. — *Getting the Deal Through: Merger Control 2008*, question 22. Available at http://www.gettingthedealthrough.com/crossborder.php?sector_id=71®ion_id=36 (30.07.2008).

³⁴ Author's conclusion on the basis of Annual Reports 2000, 2001, 2002, 2003, 2004, 2005 and 2006 of the Czech Office for the Protection of Competition. Available at <http://www.compet.cz/en/information-centre/annual-reports/> (11.05.2008). See also A. Bányaiová. Czech Republic, in *Getting the Deal Through: Merger Control 2008*, question 22. Available at http://www.gettingthedealthrough.com/crossborder.php?region_id=49§or_id=71 (30.07.2008).

³⁵ A. Economou. Greece. — *Getting the Deal Through: Merger Control 2008*, question 22. Available at http://www.gettingthedealthrough.com/crossborder.php?region_id=17§or_id=71 (30.07.2008).

³⁶ E-mail of D. Markovic-Bajalovic, President of the Serbian Commission for Protection of Competition, to the author, dated 7.03.2007.

In the case *Latvijas Mobilais Telefons/ZetCOM* (2007), concerning the merger of two Latvian mobile communication services providers, the Latvian Competition Council approved the merger, contingent on a range of behavioural commitments by the merging parties, including obligations to inform the customers about the merger, to maintain existing legal entities and brands until 2009, and to abstain from carrying out marketing measures especially aimed at attracting ZetCOM customers to the services of Latvijas Mobilais Telefons.^{*37}

In *Airport Bratislava/Wien Flughafen AG* (2006), concerning the merger of the two national airport operators, the Austrian Federal Competition Authority authorised the merger after the parties undertook certain behavioural commitments pertaining to price caps, the capacity of the Vienna airport and the slots available there, and the unbundling (in accountancy terms) of airport infrastructure services vertically (with respect to other airport businesses) as well as horizontally (with respect to the two airports). Compliance with the commitments was to be monitored by trustees (an independent air traffic expert and an independent auditor).^{*38}

In the 2002 *Agrofert Holding/Unipetrol* case, concerning the Czech market for nitrogen fertilisers, the Czech Office for the Protection of Competition accepted commitments of supply, of maintaining certain pricing conditions, and of making public announcements of price developments.^{*39} In *Bijouterie Trading Company/Swarovski Bohemia* (2004), concerning the bijouterie markets, the authority accepted commitments to maintain open and fair demand for supplies.^{*40}

2.4. Justifications for the wider use of behavioural remedies in small economies

2.4.1. Lack of enforcement power

As could be seen from section 1 of this article, in small economies many sectors are supplied by way of imported goods, and market participants often are owned by foreign companies. In such cases, the merger of foreign companies importing into or having subsidiaries in a small economy is likely to have effects on the competition conditions also there and would fall subject to control in such a small economy. In cases of cross-border mergers, particularly in the event of so-called foreign-to-foreign mergers, it may prove rather difficult for the competition authorities of small economies to take any effective enforcement actions undermining the merger or requiring compliance with burdensome conditions on the part of the merging parties.

The declaration of invalidity of a foreign-to-foreign merger would not have effects on the validity of the merger transaction if this transaction is legal in the home jurisdictions of the merging parties and under the laws chosen by the parties to apply for the transaction. Similarly, the threat of penalties would be unlikely to stop the foreign-to-foreign merger, because of the lack of adequate enforcement measures. Even if the competition authority controlling a foreign-to-foreign merger could impose sanctions on the entities of the merging parties that are active in its jurisdiction or undermine the sales of the goods of the merging parties in its territory, it would risk causing the merging companies to leave the small economy all together, which might render the local consumers worse off.

The *Unilever/Ben & Jerry's* (2000) case from the practice of the Israel Antitrust Authority provides a good illustration of such circumstances. In 2000, US company Ben & Jerry's Homemade, Inc. and Anglo-Dutch company Unilever announced an agreement under which Unilever would acquire control over Ben & Jerry's.^{*41} The merger was subject to control, *inter alia*, in Israel.

The Israel Antitrust Authority identified competition concerns in the Israeli ice cream market. The merger was cleared conditionally, after the parties undertook to distribute Ben & Jerry's ice cream in Israel through an independent distributor who would be free to determine the prices charged for the products. Moreover, the Israel Antitrust Authority required that the quality and quantity of the products be at least as high as it had been before the merger, and that any new product be made available to the independent distributor.^{*42}

³⁷ Report on the Economic Development of Latvia, December 2007. Available at <http://www.em.gov.lv/em/2nd/?cat=137&lng=en> (30.07.2008).

³⁸ Annual Report on Competition Policy Developments in Austria 2005–2006. Available at <http://www.bwb.gv.at/NR/rdonlyres/E459F1F0-439B-4B3C-8A8B-19C203B727C7/26202/Annualreport20052006final.pdf> (30.07.2008).

³⁹ Press Release of Czech Office for the Protection of Competition of 4 September 2002: "Agrofert is allowed to acquire Unipetrol". Available at <http://www.compet.cz/en/information-centre/press-releases/competition/agrofert-is-allowed-to-acquire-unipetrol/> (30.07.2008).

⁴⁰ Annual Report 2004 of the Czech Office for the Protection of Competition, p. 16. Available at <http://www.compet.cz/en/information-centre/annual-reports/> (30.07.2008).

⁴¹ Press Release of Ben & Jerry's Homemade, Inc. of April 16, 2000. Available at http://www.benjerry.com/our_company/press_center/press/join-forces.html (30.07.2008).

⁴² Conditions for the approval of the merger between Ben & Jerry's Homemade Inc. and Unilever N.V., cited through M. Gal. Competition Policy for Small Economies. Cambridge, Massachusetts, London: Harvard University Press 2003, p. 246.

This case clearly illustrates the difficult trade-offs that the competition authorities of small economies often face in the event of foreign-to-foreign international mergers, as the actual choice of measures is rather limited. Had the merger been prohibited by the Israel Antitrust Authority, there would have been a great risk that, instead of withdrawing from the transaction, the merging parties would have simply chosen to cease their activities in Israel. This would have been even more detrimental for the Israeli consumers than an anti-competitive merger. As noted by Michal S. Gal, small economies are often left only to rely on the assumption that international firms will not change their strategic decisions (such as Ben & Jerry's introduction of new products to the world market in this case) only to reduce competition in the small economy.^{*43}

In such cases, some local concerns can be mitigated via behavioural remedies. These remedies are less burdensome for the merging parties than are structural remedies; therefore, the merging parties may be more willing to agree to comply with the former than with the latter. Furthermore, behavioural commitments could be used to address the conduct directly affecting the small economy. Hence, in such circumstances the behavioural remedy might be the only remedy available to the competition authority in a small economy.

2.4.2. Preservation of efficiency gains and other benefits of a merger

Where a merger entails significant efficiency gains or other considerable public benefits, prohibition of the merger could be too stringent a remedy — in particular, where the anti-competitive effects would be outweighed by the positive effects. In such cases, structural remedies are usually the obvious choice for removing the competition problems. However, when divestitures are applied in small economies, they often imply a trade-off between enhancing competition and exploiting the potential cost-efficiencies that flow from achieving MES of production. Even if the merging entity could be broken up into smaller parts, market demand may set limits to the number of efficient units such that high concentration rates would prevail. Furthermore, structural remedies may not be effective without costly ongoing regulation after all, because (small) inefficient firms would not survive in a free market and would never grow to sizes large enough to allow them to take advantage of economies of scale.^{*44}

Moreover, divestitures may be infeasible simply because there is no suitable package to be divested without interference with the remaining activities of the companies. This may be especially true where the total size and the range of business activities of the companies involved are rather limited. This problem is likely to have a greater effect in small economies — especially in new market economies, where private companies do not yet have a long history and their size is still limited.

Even where a suitable divestiture package exists, divestitures may not be a feasible solution because of the difficulty of finding a suitable purchaser that has no significant connection to the merging parties yet possesses sufficient resources, expertise, and incentives to operate the divestiture package as an effective competitor. In small economies, where the number of market players generally is limited, finding such a purchaser may prove rather difficult. In addition, because of particularities of specific market structures, structural remedies may not address all concerns fully.

The *Valio/Kainuu, Maito-Pirkka, Aito Maito* case, from the Finnish Competition Authority's practice, provides an example of such a situation. The case concerned the acquisition by a major Finnish dairy processor, Valio, of the dairy and marketing businesses of the co-operatives Maito-Pirkka and Kainuu and that of the company Aito Maito Fin Oy.^{*45}

The Finnish Competition Authority assessed the effects of the acquisition in more than 20 product markets and found that the concentration would have resulted in the creation or strengthening of a dominant position in several of them. In the assessment of whether the concentration could be accepted, the central issue was how the purchase of raw material (raw milk) by Valio's competitors could be ensured.^{*46}

The Finnish Competition Authority cleared the merger subject to an extensive package of remedies consisting primarily of behavioural remedies such as Valio's obligations to 1) sell to competitors annually a set amount of raw milk at prices equal to the average purchase price of Valio's own dairy industry, 2) make export purchases of raw milk as referred to in point 1 on the basis of market prices and reasonably non-discriminatory export costs, 3) offer logistics services to competitors and dairy processing and packaging services for the products referred to in point 1, and 4) sell to domestic customers all of the usual domestic milk powder brands manufactured by Valio at the market prices prevailing in the EU area. In addition, Valio was to sell some of

⁴³ *Ibid.*

⁴⁴ M. Gal (Note 1), p. 1469.

⁴⁵ Case No. 1151/81/1999 of 20.06.2000. Conditional approval of the acquisition: Valio Oy/Dairy and marketing businesses of Kainuu Co-operative, Maito-Pirka Co-operative and Aito Maito Fin Oy (Dnro. 1151/81/1999, 20.06.1999, Yrityskaupan hyväksyminen ehdollisena; Valio Oy/Kainuun Osuusmeijerin, Osuuskunta Maito-Pirkan ja Aito Maito Fin Oy:n meijeri- ja markkinointiliiketoiminnot). Available at <http://www.kilpailuvirasto.fi/cgi-bin/suomi.cgi?luku=yrityskauppavalvonta/yrityskaupparatkaisut&sivu=ratk/r-1999-81-1151> (30.07.2008) (in Finnish).

⁴⁶ *Ibid.*

the acquired brands and offer the production plants or the related equipment for sale without any restrictions on use. An independent expert was appointed to monitor compliance with the commitments.^{*47}

Because of the special features of the Finnish dairy market, divestitures of the brands and production plants alone would not have remedied the decrease in competition caused by the merger. The main impediment to competition encountered by Valio was the availability of raw milk and not production capacity, since Valio obtained the raw milk from co-operatives, which, in turn, purchased the raw milk from their producer members. As the co-operatives and producers were not parties to the acquisition, it was not possible to oblige them to deliver milk to Valio's competitors. In the event of prohibition of the transaction, the milk producers would have likely switched their supplies to Valio in due course and this would have created an even greater shortage in milk deliveries for the co-operatives to be acquired.^{*48}

It appeared later that the few structural remedies attached to the merger did not produce the desired outcomes, as no competitor was interested in acquiring the brands or businesses to be divested.^{*49} However, the competitive concerns could be dealt with by means of the behavioural remedies — the transfer of raw milk to Valio's competitors was ensured with Valio's commitment to sell raw milk at Valio's own purchase price to the actual and potential competitors in the domestic market. Hence, Valio's competitors were able to balance out the decreased competition caused by the acquisition in the liquid milk market.^{*50}

Thus, in the circumstances of limited availability of structural remedies, behavioural remedies can prove invaluable tools for securing positive effects for otherwise anti-competitive mergers.

2.4.3. Monitoring issues

Both structural and behavioural remedies require a certain degree of monitoring by the competition authority. This requires resources and expertise, which can be particularly limited in the case of small economies.^{*51}

With respect to structural remedies, monitoring involves making sure that the divestiture or licensing is accomplished on time and with all due considerations as envisaged in the merger approval, as well as ensuring the viability of the business to be divested in the interim period between the competition authority's approval of the merger and the completion of the divestiture. As noted above, behavioural remedies could be used for that purpose, but this also requires monitoring resources from the competition authority. Even though the need for such monitoring is only short-term, it may pose more challenges and require more effort on the part of the competition authority than long-term monitoring of behavioural remedies would, especially since the need for intense monitoring of the divestiture process may be more unpredictable than is ongoing monitoring of conduct.

Moreover, the mistakes made in the process of divestiture are likely to have more detrimental effects than those made in the case of behavioural remedies, as divestitures are usually irrevocable and once the viability of a divestiture package has been shaken, its potential for success can be seriously undermined. At the same time, in the case of behavioural remedies, mistakes can in many cases still be rectified through further review of the commitments made by the merging parties. This is clearly demonstrated by the *A. Le Coq/Finelin* case, from the practice of the Estonian Competition Authority. The case raised competition concerns in the market for production and sale of cider in Estonia. The authority cleared the merger conditionally on the merging parties' compliance with production volume restrictions for a period of two years after the merger.^{*52} There was extremely rapid and unexpected growth in the Estonian cider market in the year following the merger, in view of which such harsh restriction turned out to be unnecessary. The limit was increased by the authority, further to the request of the merging parties.^{*53}

The help of divestiture and interim trustees can be utilised to facilitate the divestiture process and alleviate the dangers. However, hiring a trustee can increase the costs of the transaction to unacceptable proportions for the merging parties, since the transaction values are often lower in small economies as compared to those of mergers in large ones, while the monitoring costs in the case of a divestiture are not necessarily so significantly lower in the case of mergers in small economies. Moreover, small economies often have limited human

⁴⁷ *Ibid.*

⁴⁸ *Ibid.*

⁴⁹ ICN Merger Working Group (Note 20), p. 37.

⁵⁰ Yearbook 2001 of Finnish Competition Authority, pp. 28–30. Available at <http://www.kilpailuvirasto.fi/tiedostot/vuosikirja-2001-englanti.pdf> (30.07.2008).

⁵¹ OECD Background Paper (Note 1) paragraphs 32–34.

⁵² Decision No. 38-KO of 11.11.2003. Grant of permission to the concentration No. 22-ko/2003 AS A. Le Coq/OÜ Finelin (Otsus 11.11.2003 nr. 38-KO. Koondumisele nr. 22-ko/2003 AS A. Le Coq/OÜ Finelin loa andmine). Available at <http://www.konkurentsiamet.ee/public/Koondumised/Arhiiv/ko200338.pdf> (30.07.2008) (in Estonian).

⁵³ Decision No. 27-KO, 24.08.2004. Amendment of conditions of the permission of the concentration No. 22-ko/2003 AS A. Le Coq/OÜ Finelin (Otsus 24.08.2004 nr. 27-KO. Koondumisele nr. 22-ko/2003 AS A. Le Coq/OÜ Finelin loa andmine kohustuse muutmine).

resources and expertise, as noted above. In this context, the know-how necessary for efficient enforcement of divestiture conditions may be lacking.

In the case of pre-merger notification, so-called 'fix-it-first' measures could be used; with this approach, the merging parties would be allowed to complete their merger only after the completion of the divestiture. This could also add incentives for the merging parties to arrange the divestiture expediently. However, 'fix-it-first' measures are not widely used, as they are very burdensome to the parties, since they involve delays that can be detrimental for the merger transaction.

With these considerations taken into account, greater reliance on behavioural remedies in some small economies could indeed be justified. However, the concerns related to behavioural remedies — in particular, the enforcement difficulties and the need for ongoing long-term monitoring — should be accorded serious weight in decision on whether to prohibit a merger or allow it only on condition of a bulky package of behavioural remedies.

The shortcomings of behavioural remedies are demonstrated by the Austrian case *Wrigley/Joyco*. The case concerned a foreign-to-foreign merger, whereby the US Wm. Wrigley Jr. Company, one of the world's leading chewing gum producers, would merge with Joyco Inversiones, S.A., which was part of the Spanish Corporación Agrolimen S.A. Wrigley and Joyco were the two biggest producers of bubble gum in Austria, and Wrigley had strong dominance in the chewing gum sector. The Austrian competition authorities had serious concerns about predatory portfolio effects related to the merger.^{*54} Nevertheless, perhaps because this was a foreign-to-foreign merger, the Austrian Cartel Court approved the merger, conditionally on a behavioural commitment obliging Wrigley to maintain Joyco's brands in the market for bubble gum in Austria for the following two years in order to ensure product diversity. To specify the Joyco brands concerned, Wrigley submitted a product list to the Cartel Court. Two years later, the Austrian authorities found out that Wrigley had not complied with the remedy. This non-compliance triggered initiation of proceedings for fining Wrigley.^{*55}

Regardless of the generally recognised enforcement difficulties related to behavioural remedies, it could be argued that in certain respects the small size of an economy could make the monitoring of compliance with behavioural remedies easier, as there are fewer market players and the number of cases is smaller, which makes deviations from the imposed remedies more readily detectable because of what might be termed the 'everybody knows everyone' phenomenon.^{*56} At the same time, as noted above, in many cases the resources available to competition authorities in small economies are also more limited, which, in turn, poses problems for monitoring.

Hence, the effect of smallness on monitoring is varied and is greatly influenced by the specific circumstances of any given merger.

3. Conclusions

It should be recognised that, even though competition rules around the world tend to be driven largely by the same rationale and are therefore rather uniform as compared to many other areas of law (for instance, family law or inheritance law), one size does not necessarily fit all. Common-sense flexibility is required in merger control, because of the enforcement priorities influenced by the inherent values of the society concerned and the specific characteristics of the economy, be it small or large.

Smallness of an economy has a tendency to create high concentration and high entry barriers in many industries. However, in the context of open trade and globalisation, such effects of smallness are decreasing.

This article has analysed the implications of smallness for merger remedies, questioning whether the principles applicable to the use of merger remedies in large economies are equally appropriate in small economies. It can be concluded that small economies should indeed be guided by somewhat different principles than larger economies.

The large competition law regimes have strong preference for structural remedies, applying behavioural remedies only exceptionally. In small economies, greater flexibility is needed. This is because small economies may face difficulties in enforcing prohibitions or stringent structural remedies, stemming from their weak bargaining position *vis-à-vis* large international firms, particularly in cases of foreign-to-foreign mergers. Furthermore, structural remedies may not be available or would disproportionately reduce the efficiency gains or other public benefits related to the merger. In addition, even though enforcement of structural remedies

⁵⁴ Annual Report on Competition Policy Developments in Austria 2003–2004, p. 14. Available at <http://www.oecd.org/dataoecd/36/33/34720199.pdf> (30.07.2008).

⁵⁵ Annual Report on Competition Policy Developments in Austria 2005–2006. Available at <http://www.bwb.gv.at/NR/rdonlyres/E459F1F0-439B-4B3C-8A8B-19C203B727C7/26202/Annualreport20052006final.pdf> (30.07.2008).

⁵⁶ OECD Background Paper (Note 1) paragraph 32.

is generally considered easier than enforcement of behavioural remedies, this may not always be true in the case of small economies.

In general, the effects of smallness in the context of merger remedies can take many forms. Also, of course, much depends on the specific circumstances of the merger under consideration and, more broadly, on the market conditions and other particularities of the economy in question.



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Some Issues of the Estonian Innovation and Intellectual Property Policy^{*1}

1. Introduction

The global economic trends characterised as the transformation into a knowledge-based economy have had remarkable implications for entrepreneurs and the society at a larger level. The Estonian business environment is no exception. The main consequences of this transformation are that knowledge is perceived as a valuable commercial asset and innovation has become a core process for value creation within a knowledge-based economy and a means for tackling social and environmental problems. Since protection of intellectual property (IP) constitutes an essential condition for innovation, the transformation has had an impact on the IP system as well. As a result, the enhancement of innovation should be regarded as a central IP system objective. Therefore, the value of an intellectual property system lies in its ability to foster innovation.

In this article, the author analyses some aspects of innovation and intellectual property policy that need to be considered to support innovation in Estonia. For the purpose of this article, innovation policy refers to actions taken to extend and accelerate innovation. Intellectual property policy forms an integral part of innovation policy.

The author suggests that innovation and IP policy is country- and region-specific, which means that almost every country and region has its unique conditions that need to be considered in designing innovation and intellectual property policy measures. The article focuses mostly on some essential aspects of Estonian IP policy.

The paper addresses problems related to IP protection at two levels: the first level concerns state-level IP policy, and the second level of discussion addresses actions that Estonian entrepreneurs may be able to take to enhance their IP competencies and foster innovation.

The author presumes that the profile of Estonian entrepreneurs should be considered in the design of the state-level IP policy. The author suggests that utility models and trade secret protection are very useful IP tools for Estonian entrepreneurs and therefore it would be appropriate to review critically the existing regulations on utility models and trade secrets.

The author recommends that, in addition to state-level IP policy measures, there must be entrepreneurs developing their IP competencies. Entrepreneurs could start with the adoption of internal IP regulations that address issues such as ownership of IP created during employment, strategies for managing IP, and the like.

¹ This research has been partially financed by the EU Commission, in Framework Programme 6, Priority 7 on "Citizens and Governance in a knowledge based society", contract No. CIT5-028519. The author is solely responsible for the contents which might not represent the opinion of the Community. The Community is not responsible for any use that might be made of the data appearing in this publication.

2. Interrelation of innovation and intellectual property

The term 'innovation' is derived from the Latin word *innovare*, which means 'to renew'. As a rule, policy documents and legal acts do not provide an exhaustive and universal definition of innovation. For instance, in EU documents, the terms 'innovation' or "innovation in a broad sense"² is used. The Estonian Research and Development and Innovation Strategy³ (more simply referred to as the Estonian innovation strategy) describes activities that could be summarised as innovation: "Innovation includes implementation of the latest results of scientific research as well as existing knowledge, skills, and technologies in an innovative manner."⁴ Section 2 of the Organisation of Research and Development Act⁵ defines innovation as "the utilisation of new ideas and knowledge in order to implement innovative solutions". The definitions referred to seem to exclude knowledge creation by means of innovation. The author argues that knowledge production constitutes an integral part of innovation. It is not reasonable to assume that knowledge comes from somewhere else and innovation means only its implementation. For the purpose of this article, the author defines innovation as a process that includes both creation of knowledge and its subsequent utilisation.

Objectives of innovation can be analysed from different perspectives. The most visible and noticeable outcomes of innovation are new products and services. The purpose of innovation, however, is not limited to the creation of commodities. Innovation is also believed to have an impact on the economy. Therefore, it has been suggested that innovation is "one of the most important factors in economic competition".⁶ It is possible to place innovation in an even broader context by arguing that it generates wealth and tackles social and environmental problems. Supporting innovation is seen as a way to surmount challenges (problems related to ageing populations, environmental issues, mounting competition, etc.) facing Europe. At least the European Commission believes so: "innovation in a broad sense is one of the main answers to citizens' material concerns about their future".⁷ Not surprisingly, innovation is sometimes thought to be one of the factors influencing the world's future trends.⁸

In view of the complexity of the objectives of innovation and the fact that innovation policy can be implemented on different levels (e.g., regional, country, sector, and industry levels), it becomes evident that innovation policy encompasses a variety of components. Therefore, in order to enhance innovation, it is necessary to invest in human capital, improve the legal framework, stimulate business research, facilitate knowledge transfer from academia to industry, etc. Depending on the implementation levels and specific objectives, the role and importance of innovation policy measures vary. However, the author assumes that protection of intellectual property constitutes an essential condition for innovation.

Intellectual property is traditionally defined as legal rights resulting from intellectual activity.⁹ The traditional approach places IP in a legal context. The role of intellectual property, however, has changed. Knowledge as a subject of IP protection has become a valuable commercial asset to many firms, other organisations, and individuals. This development has shifted the emphasis from the legal aspect of IP (that is, IP as legal rights) to its economic aspect (IP as a commercial asset). Consequently, intellectual property is considered rather more as an economic asset than in terms of legal rights. The author argues that the contemporary notion of IP should incorporate both — the economic (IP as an asset) and legal (IP as rights) aspects.¹⁰ Without any doubt, it is important to acknowledge the economic nature of intellectual property and its interrelation with innovation. At the same time, the legal nature of IP is no less important. The great relevance of the legal aspect of intellectual property is caused by the fact that knowledge by nature is a public good.¹¹ This means that knowledge

² Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions. Putting knowledge into practice: A broad-based innovation strategy for the EU – COM(2006) 502, 13.09.2006, p. 2.

³ Knowledge-based Estonia. Estonian Research and Development and Innovation Strategy 2007–2013. Available at <http://www.hm.ee/index.php?0&popup=download&id=6175> (10.11.2007).

⁴ *Ibid.*, p. 9.

⁵ Teadus- ja arendustegevuse korralduse seadus. Entered into force on 2.05.1997. – RT I 1997, 30, 471; 2007, 12, 66 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (14.05.2008).

⁶ M. Pohlmann. The Evolution of Innovation: Cultural Backgrounds and the Use of Innovation Models. – Technology Analysis & Strategic Management 2005 (17) 1, p. 9.

⁷ Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions. Putting knowledge into practice: A broad-based innovation strategy for the EU – COM(2006) 502, 13.09.2006, p. 2.

⁸ E. R. Peterson. Seven Revolutions: Global Strategic Trends Out to the Year 2025. – The Multinational Business Review 2004 (12) 2, p. 111.

⁹ See Article 2 (viii) of the Convention establishing the World Intellectual Property Organisation. Stockholm, 14.07.1967, entered into force in respect to Estonia on 5.02.1994. – RT II 1993, 25, 55.

¹⁰ For further discussion see A. Kelli, H. Pisuke. Intellectual Property in an Innovation-based Economy. – Review of Central and East European Law 2008 (33) 2, pp. 223–238.

¹¹ For further discussion see B. Andersen. If 'intellectual property rights' is the answer, what is the question? Revisiting the patent controversies. – Economics of Innovation and New Technology 2004 (13) 5, pp. 417–442.

does not have any attributes that could facilitate the exclusion of others from exploiting it. In the absence of an adequate protection, any investment made in creation of new knowledge is prone to become lost. Since the economic system does not offer sufficient control mechanisms to protect the valuable knowledge generated, it is up to the legal system to fill the gap. The IP system provides legal tools to control the utilisation and commercialisation of the knowledge created. Analysing the essence of IP, one can state that, despite the fact that the utilisation of knowledge takes place in business settings, the control over it is established by the legal system. To sum up, the term 'intellectual property' in this article refers to a combination of the economic (an asset) and legal (rights) concepts. To emphasise the legal aspect of intellectual property, the author uses the term 'intellectual property rights' or the abbreviation 'IPRs'.

The EU innovation strategy is based on the assumption that protection of intellectual property is a *sine qua non* for innovation.^{*12} It is obvious that profit-oriented actors are interested in securing their investments.^{*13} Intellectual property is certainly a suitable tool to package some results of innovation. Therefore, the European Commission assumes the existence of a correlation between the use of IPRs and good innovation performance.^{*14}

In order to analyse correlation between the use of IPRs and innovation performance, one must first highlight some key elements. The mere existence of a large number of IPRs does not necessarily represent outstanding innovation performance. Still, some policy documents prioritise formal indicators such as the number of patents granted. For instance, the strategy document 'Estonian Success 2014' sets forth the following objective: "[T]he number of patents registered per 100,000 inhabitants in Estonia will be multiplied by 10".^{*15} The author personally has doubts regarding formalistic goal-setting. A high number of IPRs neither guarantees wealth generation nor certifies innovation performance as excellent. Furthermore, it is also useful to take into account that the number of IPRs could be influenced by other factors and trends. For instance, K. Hussinger hypothesises that "the increase in patents rather is motivated by their heightened strategic value".^{*16} In other words, the growing use of IPRs is not necessarily a result of improved innovation performance and a substantial rise in R&D investments; it could reflect a change in business behaviour. The underlying cause of the changed behaviour might be that business actors have started to regard knowledge as a valuable asset that has to be protected. This line of reasoning is supported by Estonian economists, stating that, among other things, "[t]he growing role of knowledge intensity in the economy is also reflected in the explosive growth in the use of different means of intellectual property protection".^{*17}

Despite the fact that innovation and intellectual property are intertwined with each other in a rather complex way, the use of IP instruments — patents, in particular — could shed some light on the intensity, extent, and direction of innovation. Since knowledge production is costly, there is a need for protection. Consequently, knowledge is packaged in the form of IPRs (e.g., patents). On account of the design of IP instruments (e.g., disclosure requirements in patenting procedure), outcomes of innovation become visible. Therefore, patent information is a primary source providing valuable insights into emerging technologies as well as trends of innovation. The high costs associated with patents (registration, maintenance, possible infringement suits, etc.) should at least in theory ensure that only the most advanced core technologies are patented. Today's reality is, however, that the majority of patents protect incremental rather than breakthrough inventions. Still, patent databases provide a good overview of innovation. Information concerning the utilisation of IPRs supports the development of models to investigate correlation patterns of IP and innovation.

^{*12} Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions. Putting knowledge into practice: A broad-based innovation strategy for the EU – COM(2006) 502, 13.09.2006, p. 6.

^{*13} In addition to acquiring intellectual property rights, it is also possible to protect investments in innovation by relying on a short innovation cycle, effects of learning curve, advantages of economies of scale, natural or statutory monopolies, etc. A strategic decision to use only IP-based instruments, combine IP tools with other mechanisms or rely solely on other mechanisms depends on a variety of sector-specific factors.

^{*14} Communication from the Commission to the European Parliament and the Council. Enhancing the patent system in Europe – COM(2007) 165, 3.04.2007, p. 2.

^{*15} Eesti Edu 2014. Vabariigi Valitsuse strateegiadokument (Estonian Success 2014. Strategy document of the Government of the Republic). Available at <http://www.riigikantselei.ee/failid/EE2014.doc.pdf> (19.03.2008), p. 10 (in Estonian).

^{*16} K. Hussinger. Is Silence Golden? Patents versus Secrecy at the Firm Level. – Economics of Innovation and New Technology 2006 (15) 8, p. 737.

^{*17} T. Mets, M. Leego, T. Talpsep, U. Varblane. The Role of Intellectual Property Protection in the Business Strategy of University Spin-Off Biotech Companies in a Small Transition Economy. – Review of Central and East European Law 2007 (32), p. 20.

3. Implications of a specific innovation context for the design of IP policy

General objectives and basic principles of innovation are usually similar in all regions and countries. As a rule, innovation is expected to advance physical, social, economic, and environmental welfare. However, the policy measures to achieve the objectives and implement underlying principles of innovation may differ substantially from one national or regional context to the next. Therefore, it has been argued that the transfer of successful regional models for innovation to a different national context fails on account of the lack of their institutional embedding.^{*18} The author agrees that framework conditions for innovation are essentially unique in every country and fostering innovation requires tailor-made solutions. In this section of the paper and those that follow, the author addresses some selected issues that need to be considered in the design of innovation and IP policy measures on country and company level.

Toomas Luman, the president of the Estonian Chamber of Commerce and Industry, has pointed out that in order to design appropriate innovation policy it is crucial to consider the profile of Estonian entrepreneurs.^{*19} According to the official statistics prepared by Statistics Estonia, the profile of Estonian enterprises by number of employees in 2007 was as follows^{*20}:

Enterprises in the statistical profile by year and number of employees

	More than 250	50–249	10–49	Fewer than 10
2007	187	1,379	7,187	67,406

Note: Economically active sole proprietors registered in the Commercial Register, excl. economically active sole proprietors registered only in the Register of Taxable Persons.

From statistical data, we know that the majority of Estonian entrepreneurs' undertakings are small and medium-sized enterprises (SMEs).^{*21} This gives rise to the question of whether the profile of Estonian enterprises has an impact on the design of innovation and intellectual property policy. The author is convinced that it does. For reasons of space, the subsequent analysis is confined to consideration of the implications of firm size for IP policy.

The author suggests that the size of an enterprise could influence its capabilities to create, acquire, manage, and utilise proprietary knowledge. The suggestion is based on the assumption that the resources invested in the creation or acquisition of new knowledge (innovative solutions) are independent of firm size. Bigger firms could even reap the benefits of economies of scale and gain advantage from their absorptive capacity. Furthermore, the cost of innovation is not influenced by the subsequent utilisation of the knowledge created. This means that the expenses of developing a product are virtually the same whether for local, regional, or global markets. However, because of the intangible nature of knowledge, entrepreneurs are motivated to exploit it to the maximum extent. When the use of tangible property has limits (e.g., I can use my phone myself or hire it out to someone else, but exercising these two exploitation options simultaneously is not physically possible), then the concurrent exploitation of intangible property is a potential option (I can use my invention myself and license it to someone at the same time). Consequently, enterprises are striving to commercialise their proprietary knowledge in as many markets as possible. To facilitate the process of commercialisation, knowledge is usually packaged in the form of IP (e.g., in the form of patents). Successful commercial exploitation of knowledge is heavily dependent on efficient IP management. It is obvious that large firms are better equipped to manage their IP than small ones are. Of course, there are some exceptions. Still, the superior management capabilities of bigger enterprises result in higher returns, which can be reinvested in knowledge creation or access (e.g., licensing). Small firms, on the other hand, lack the necessary resources for conducting R&D, which is a primary

¹⁸ M. Pohlmann (Note 6), p. 9.

¹⁹ T. Luman, Teadus- ja arendustegevus ning majanduse konkurentsivõime. Probleemid, areng ja suundumused (Research and Development Activities and Competitiveness of Economy. Problems, Developments and Trends). – Tehnoloogia ja teadmussuure konverents. Ettevõtlike ülikoolide teenused – teaduspõhine koostöö (Conference on Technology and Knowledge Transfer. Services of Enterprising Universities). 24.01.2008.

²⁰ Information available at <http://pub.stat.ee/px-web.2001/Dialog/SaveShow.asp> (29.04.2008).

²¹ Pursuant the EU policy document "[t]he category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million". See Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/361/EC). – OJ L 124, 20.05.2003, p. 36–41.

input of innovation.^{*22} Even if the research activities of a small company lead to a breakthrough invention, it is highly unlikely that the firm can market it regionally and globally on its own. The decisive issue here is the ability of the company to protect and enforce its rights. The protection of rights usually takes place in court, which is rather costly, especially when enforcement is required in different jurisdictions. The same concern has been raised in the theoretical literature as well: "High litigation costs are particularly destructive of the contributions to innovation that smaller firms have proved they can make. It is obvious that the measurable costs of prosecuting or defending an action for patent infringement are far beyond the resources of all but the largest firms, apart from the fact that the burden of the costs that cannot be measured (such as distraction from more immediately paying tasks) falls most heavily on smaller ones."^{*23}

The aim of the above discussion is not to say that SMEs cannot be innovative, or that innovation and IP policy should disregard them. The author feels quite the opposite. The main concern is whether an innovation and IP policy designed mainly for big companies and IP tools used by large corporations meet the needs of small enterprises. Understandably, concrete IP policy cannot be based only on formal characteristics such as the size of the firm involved. There are also suggestions in the literature that "[f]irm size affects the probability to introduce an innovation, but it is less important in affecting the innovation strategy followed by firms. Most of the differences between the innovation behaviours and performances of large and small firms are, therefore, due to compositional effects, that is, to the fact that large corporations tend to concentrate in highly innovative industries (and countries), whereas small firms concentrate in more traditional sectors."^{*24} Therefore, it would also be necessary to monitor the dynamics of patent applications and patents granted to Estonian enterprises. Analysis of patenting trends could provide a basis for identification of emerging innovative sectors and development of measures to support these sectors.

In addition to state-level policy measures, there are certain steps that Estonian entrepreneurs can take themselves for improved competitiveness. The key issue here is the adoption of an appropriate innovation model. It is possible to distinguish between different approaches to innovation on company level. One possible way to manage innovation is that of a single company trying to control its entire process of creation of value from knowledge. H. W. Chesbrough refers to this model as the Closed Innovation. According to Chesbrough, the Closed Innovation is an internally focused approach, one that requires companies to generate their own ideas and then develop and commercialise them on their own. The Closed Innovation approach expects entrepreneurs to be self-reliant.^{*25} It is obvious that, in order to be a successful actor in the framework of the Closed Innovation, an entrepreneur needs a considerable amount of resources. Since small companies lack financial strength, they cannot effectively be involved in innovation. However, there is another way to manage innovation. It is called Open Innovation. Chesbrough describes it as follows: "Open Innovation means that valuable ideas can come from inside or outside the company and can go to market from inside or outside the company as well. This approach places external ideas and external paths to market on the same level of importance as that reserved for internal ideas and paths to market during the Closed Innovation era."^{*26} As described above, the logic of Open Innovation does not require an entrepreneur to capture value in the construction of an entire value chain on its own. A high proportion of the value can be claimed for fulfilment of some key functions (e.g., generation of new knowledge, adding useful features to existing products, etc.) within a value chain. The approach of Open Innovation is especially relevant for small companies, since it allows them to operate with only modest resources. Considering the profile of Estonian enterprises, one can see several advantages of Open Innovation for them.

In the following sections of the paper, the author discusses possible implications of the profile of Estonian enterprises for IP policy. First the author concentrates on state-level IP policy, before exploring possible company-level actions to foster innovation.

²² It is necessary to emphasise that R&D expenditure is not the only characteristic of innovative firms. R. Evangelista and V. Mastrostefano conclude correctly that "the innovation strategy of firms cannot be defined only through their commitment to R&D. Other activities such as the design and the acquisition of know-how and training do differentiate the innovative behaviours of firms and the technological profile of industries." See R. Evangelista, V. Mastrostefano. *Firm Size, Sectors and Countries as Sources of Variety in Innovation*. – *Economics of Innovation and New Technology* 2006 (15) 3, p. 266.

²³ W. Kingston. *Innovation needs patents reform*. – *Research Policy* 2001 (30), p. 410.

²⁴ R. Evangelista, V. Mastrostefano (Note 22), p. 267.

²⁵ H. W. Chesbrough. *Open Innovation: The New Imperative for Creating and Profiting from Technology*. Harvard Business School Press 2003, p. XX.

²⁶ *Ibid.*, p. 43.

4. Proposed areas of focus for Estonian IP policy

4.1. State-level IP policy

Estonia has adopted the major IP-related international legal instruments. For instance, Estonia is a signatory to the Paris Convention for the Protection of Industrial Property^{*27}, the Berne Convention for the Protection of Literary and Artistic Works^{*28}, and the Agreement on Trade-Related Aspects of Intellectual Property Rights^{*29} (the TRIPS agreement). Estonia is also a party to key regional agreements in the field of IP (such as the European Patent Convention^{*30}) and has harmonised its legislation with the corresponding EU directives in the field of IP. Therefore, it could be said that the general legal framework for IPRs in Estonia does not differ substantially from that in highly developed and innovative European countries (e.g., Sweden, Finland, Germany, and Denmark). Still there is a remarkable difference in R&D investments as a primary input to innovation when one compares Estonia to the countries mentioned. In 2006, gross domestic expenditure on R&D as a percentage of the gross domestic product was 3.73% in Sweden, 3.45% in Finland, 2.53% in Germany, 2.43% in Denmark, and 1.14% in Estonia.^{*31}

A co-ordinated effort spanning many years definitely is going to be required of public and private stakeholders alike before Estonia can reach a comparable R&D investment level. For instance, it is crucial to support university and business research in technical fields and the life sciences. If new knowledge is created by university researchers, it is vital to assure that other stakeholders in a knowledge-based economy can utilise it. For reasons of space, it is not possible to consider all necessary actions on these pages. In this section, the author discusses only some state-level IP policy measures. The author's main argument here is that, even though Estonian intellectual property regulations are mostly based on international and EU principles, it is still possible to adjust them to the Estonian economic context, which could in the end foster innovation. The author would also like to emphasise that even an excellent legal framework for IPRs is useless unless entrepreneurs and other stakeholders are aware of it.

The author is convinced that a key issue of innovation policy is the creation of IP awareness. Special measures have to be designed for different target groups (university students, entrepreneurs, etc.). In order to raise the level of IP awareness of those who will contribute to the construction of a knowledge-based economy, it is crucial that a general course on IP be made compulsory for all university students. In some fields (among them law, economics, engineering, and the biological sciences), students should be offered advanced courses on IP. When it comes to entrepreneurs, special attention in promoting IP awareness (e.g., through training and consultancy) should be paid to economic exploitation of intellectual property. In addition to understanding the basics of IP, entrepreneurs have to acknowledge their need for IP competencies. In the context of this paper, IP competencies are defined as skills that are crucial for creating, protecting, and commercialising intellectual property, as well as for managing it in the intellectual value chain.^{*32} Put differently, entrepreneurs require capabilities to construct IP-based business models, develop their IP strategy, evaluate IP, etc.

Besides traditional methods of increasing IP awareness (training and courses, consultancy services, etc.), case law could also be considered as an efficient mechanism to enhance IP awareness, particularly among lawyers and entrepreneurs. Case law evolves alongside the economy and provides market participants with valuable guidelines and feedback for evaluating their business strategies, including IP strategies.

Estonian IP-related case law is not very extensive, and only a few cases have addressed protected inventions. There are still some landmark decisions, however. For instance, the case *AS Balteco v. AS Neoqi* decided by the Estonian Supreme Court is quite explicit as to what happens to entrepreneurs who do not manage their productive knowledge properly. In this case, some ex-employees of AS Balteco established the company AS Neoqi, which started to manufacture products similar to those of AS Balteco. Additionally, AS Neoqi protected its product as a utility model. Even though AS Balteco claimed that its trade secrets were misused and the utility model was invalid (allegedly, it lacked novelty and an inventive step), the Estonian Supreme Court did not support these claims.^{*33} The case shows that it is not enough if we treat IP as an asset; we should also

²⁷ Paris Convention for the Protection of Industrial Property. Paris, 20.03.1883, entered into force in respect to Estonia on 24.08.1994. – RT II 1994, 4–5, 19.

²⁸ Berne Convention for the Protection of Literary and Artistic Works. Berne, 9.09.1886, entered into force in respect to Estonia on 26.10.1994. – RT II 1994, 16–17, 49.

²⁹ Agreement on Trade-Related Aspects of Intellectual Property Rights. Marrakech, 15.04.1994, entered into force in respect to Estonia on 13.12.1999. – RT II 1999, 22, 123.

³⁰ Convention on the Grant of European Patents. München, 5.10.1973, entered into force in respect to Estonia on 1.07.2002. – RT II 2002, 10, 40.

³¹ Eurostat. Gross domestic expenditure on R&D as a percentage of GDP. Available at http://epp.eurostat.ec.europa.eu/portal/page?_pageid=1996,39140985&_dad=portal&_schema=PORTAL&screen=detailref&language=en&product=REF_SI_IR&root=REF_SI_IR/si_ir/tsiir020 (18.07.2008).

³² IP Knowledge Centre within the ScanBalt BioRegion (2003), project No. 02150, p. 15.

³³ CCSCd 16 November 2005, in matter 3-2-1-115-05. – RT III 2005, 40, 400 (in Estonian).

establish control over it by packaging knowledge as a patent or utility model or another IPR form. It is also crucial to take the steps necessary to protect one's trade secrets.

The next required measure taken simultaneously with creation of awareness is to design and fine-tune IP tools that correspond to the actual needs of Estonian entrepreneurs. As shown above, the majority of Estonian entrepreneurs are very small enterprises. The following analysis concentrates mainly on utility models, patents, and trade secrets and their role for small businesses.

The author suggests that utility models could be useful IP tools for SMEs for a variety of reasons. Subsection 5 (1) of the Utility Models Act³⁴ defines utility models as "inventions that are new, that involve an inventive step, and that are susceptible to industrial application". Utility models have lower inventive step thresholds than do patents, which makes them particularly suitable for small companies. An important role of utility models has also been acknowledged in the theoretical literature. For instance, W. Cornish & D. Llewelyn emphasise that "industry needs a system of short-term rights protecting minor technical advances, which supplements the patent system and is particularly valuable where know-how cannot be kept secret".³⁵ The author of the present work presumes that the role of utility models is not limited to protecting incremental inventions. Positive features of utility models (e.g., the lesser inventive step requirement, the affordable registration fees, and efficient protection) could lead to wide acceptance of this IP tool by entrepreneurs. All of this would create a good environment to enhance IP culture among Estonian enterprises. After development of capabilities to manage utility models, it would be easier to realise the potential of the patent system. Therefore, the author suggests analysis of the existing regulation on utility models and its practical implementation to identify and tackle potential problems. It would also be advisable to further develop mechanisms encouraging and supporting the use of utility models. In addition, the author would welcome the substantial harmonisation of the regulation on utility models at the EU level. Since business activities of even small firms are not always confined to the territory of a state, the absence of a similar legal framework might become an obstacle to value creation via innovation.

As a general rule, patents are not considered suitable IP tools for SMEs. For instance, W. Kingston argues that the patent system "serves small firms, which have most need of effective protection for their inventions, particularly badly".³⁶ K. Hussinger seems to support this position by arguing that "patents are used where the expected monopoly profits are large".³⁷ There are also surveys that show that small enterprises prefer specific IP tools. For instance, "small firms, on average, do not rely more on patents than on secrecy in comparison with large firms. Instead, small firms are less likely than large firms to find patents to be of greater value than secrecy for product innovations, although there is little difference by firm size for process innovations".³⁸ The discussion above indicates that it would be appropriate to review critically the existing legal mechanisms for protection of trade secrets³⁹, especially in economies largely composed of SMEs. The author's intention is not to suggest that the Estonian economy does not need a patent system. In fact, the author is convinced that a patent system is an essential condition for innovation. The main argument here is that an efficient mechanism for legal protection of trade secrets and a functioning patent system could complement each other. In addition, strong protection for trade secrets would benefit not only SMEs but also large corporations. Even for big companies, it is not always useful to patent inventions (e.g., if market exploitation of the inventions is very far off or the inventions relate to a process). In the cases described, secrecy could be a good option.

Legal protection of trade secrets is regulated by a number of legal acts in Estonia. Since Estonia is a party to several IP-related international agreements, it is necessary to consider the regulation material of these as well. For instance, Article 39 of the TRIPS agreement establishes a general framework for protection of undisclosed information.⁴⁰ Sections 50 and 52 of the Competition Act⁴¹ address misuse of confidential information prohibited as unfair competition. Section 50 of the Republic of Estonia Employment Contracts Act⁴² obliges an

³⁴ Kasuliku mudeli seadus. Entered into force on 23.05.1994. – RT I 1994, 25, 407; 2007, 13, 69 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

³⁵ W. Cornish, D. Llewelyn. *Intellectual Property: Patents, Copyright, Trade Marks and Allied Rights*. 6th edition. London: Sweet & Maxwell 2007, p. 10.

³⁶ W. Kingston (Note 23), p. 411.

³⁷ K. Hussinger (Note 16), p. 751.

³⁸ A. Arundel. The relative effectiveness of patents and secrecy for appropriation. – *Research Policy* 2001 (30), p. 622.

³⁹ In this article the terms 'trade secret', 'know-how', 'undisclosed information' and 'confidential information' are regarded as synonyms.

⁴⁰ Pursuant to the referred article of the TRIPS agreement "persons shall have the possibility of preventing information lawfully within their control from being disclosed to, acquired by, or used by others without their consent in a manner contrary to honest commercial practices so long as such information: (a) is secret in the sense that it is not, as a body or in the precise configuration and assembly of its components, generally known among or readily accessible to persons within the circles that normally deal with the kind of information in question; (b) has commercial value because it is secret; and (c) has been subject to reasonable steps under the circumstances, by the person lawfully in control of the information, to keep it secret".

⁴¹ Konkurentsiseadus. Entered into force on 1.10.2001. – RT I 2001, 56, 332; 2007, 66, 408 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

⁴² Eesti Vabariigi töölepingu seadus. Entered into force on 1.07.1992. – RT 1992, 15/16, 241; 2007, 44, 316 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

employee to maintain the business and production secrets of the employer. Sections 186, 313, and 325 of the Commercial Code^{*43} provide that the members of the management and supervisory board shall preserve the business secrets of the company. Sections 372 and 625 of the Law of Obligations Act^{*44} require a licensee and a mandatary to maintain the confidentiality of information of which they become aware in connection with the fulfilment of the agreement.

The author is of the opinion that, on account of a presumption of high strategic relevance of trade secret protection to Estonian entrepreneurs, regulations on trade secrecy could be more detailed. Even adoption of a special legal act (e.g., a 'Trade Secrets Act') should be considered. The scope of information protected as trade secrets need not be necessarily extended. Rather, the main issue is to specify protection criteria, the legal status of trade secrets developed by an employee, procedural issues (e.g., the burden of proof), etc. The design of effective legal measures to protect confidential information requires a comprehensive understanding of the economic context of trade secret misappropriation. Legal acts and contracts forbid an employee or other person (e.g., a party to some contract, a management board member, or the like) who becomes aware of a trade secret during employment or fulfilment of his or her contractual obligations from revealing or using it. A company's unlawful exploitation of someone else's trade secret is generally regarded as unfair competition, which is prohibited by law. To sum up, the measures to protect trade secrets are applied on two levels: on the first level, an employee or other person is obliged to maintain somebody else's trade secret, and on the second level entrepreneurs (usually competitors) are forbidden to obtain a rival's trade secret by means of dishonest commercial practices. In a dispute, the measures described may turn out to be ineffective. Elise Vasamäe has raised a relevant issue related to the existence of effective legal protection measures in the case where it is obvious that a competitor is using a rival company's trade secret but the latter is not able to prove that the trade secret was acquired by dishonest means (e.g., from an employee of the rival company).^{*45} Without any doubt, all entrepreneurs should create strategies to protect their IP (including trade secrets). These strategies should include routines to map existing trade secrets, even establishing platforms for digital management of documents containing trade secrets. However, the reality is that SMEs might not have the resources to do so. One possible solution might be that if a company discovers that a competitor is exploiting its trade secret and other circumstances suggest that it was obtained unlawfully (e.g., from an employee of the company) the competitor would be required to prove the origin of the trade secret. A similar approach is used to protect process patents.^{*46} Still the proposal requires further analysis since reversal of the burden of proof as described could create many new problems (for example, in order to find out more about a competitor's trade secret, it would be enough simply to accuse the competitor of stealing your trade secret).

4.2. A need to enhance the IP competencies of Estonian entrepreneurs

Statistical information shows us that Estonian gross domestic expenditure on R&D as a percentage of the gross domestic product was 0.93% in 2005 and 1.14% in 2006.^{*47} The percentage of the total R&D expenditure borne by Estonian industry was 38.5% in 2005 and 38.1% in 2006. In other European countries, the percentage of gross domestic expenditure on R&D financed by industry was 65.7% in Sweden, 66.9% in Finland, 67.6% in Germany, 59.5% in Denmark, 79.7% in Luxembourg, 20.8% in Lithuania, and 34.3% in Latvia in 2005.^{*48}

The data can reveal several relevant facts. Firstly, there has been growth in Estonian R&D expenditure. Secondly, Estonian entrepreneurs have not increased their investments in R&D. Finally, industry in developed countries accounts for a greater share of R&D investments. The author suggests that, because of the changes taking place in the Estonian economy^{*49}, Estonian entrepreneurs increasing their R&D spending is inevitable.

⁴³ Äriseadustik. Entered into force on 1.09.1995. – RT I 1995, 26–28, 355; 2007, 67, 413 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

⁴⁴ Võlaõigusseadus. Entered into force on 1.07.2002. – RT I 2001, 81, 487; 2007, 56, 375 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (30.04.2008).

⁴⁵ A communication with Elise Vasamäe during the author's presentation in IP seminar held by Professor Norbert Reich (26.04.2008).

⁴⁶ Article 34 of the TRIPS agreement sets out the following principle: "if the subject matter of a patent is a process for obtaining a product, the judicial authorities shall have the authority to order the defendant to prove that the process to obtain an identical product is different from the patented process".

⁴⁷ Eurostat. Gross domestic expenditure on R&D as a percentage of GDP. Available at http://epp.eurostat.ec.europa.eu/portal/page?_pageid=1996,39140985&_dad=portal&_schema=PORTAL&screen=detailref&language=en&product=STRIND_INNORE&root=STRIND_INNORE/innore/ir021 (12.04.2008).

⁴⁸ Eurostat. Gross domestic expenditure on R&D by source of funds — industry. Available at http://epp.eurostat.ec.europa.eu/portal/page?_pageid=1996,39140985&_dad=portal&_schema=PORTAL&screen=detailref&language=en&product=STRIND_INNORE&root=STRIND_INNORE/innore/ir022 (12.04.2008).

⁴⁹ See U. Varblane *et al.* Eesti majanduse konkurentsivõime hetkeseis ja tulevikuväljavaated. Aruanne tellitud Eesti Arengufondi poolt (Current Competitive Status and Prospects of the Estonian Economy. Report ordered by the Estonian Development Fund). Available at http://www.arengufond.ee/files/ty_raport.pdf (12.04.2008) (in Estonian).

The Green Paper on the European Research Area also emphasises that “[t]he business sector is supposed to contribute two-thirds of the 3% of GDP R&D intensity target”.⁵⁰ Besides investing more in knowledge production, Estonian entrepreneurs need to enhance their IP competencies in order to manage the outcomes of innovation effectively. In this section of the article, the author analyses some IP-related issues that entrepreneurs have to consider in their everyday business.

One of the objectives of doing business is to make a profit. Economic reality is that services and products used for creation of wealth are becoming increasingly knowledge-intensive. Therefore, it has been suggested that the three traditional factors of production (land, labour, and capital) are overshadowed by knowledge.⁵¹ B. Andersen has explained this further: “The battles are not for control of raw materials, but for the control of the most dynamic strategic asset, namely ‘productive knowledge’.”⁵² Thus it can be argued that it is vitally important for an entrepreneur to enhance and protect its productive knowledge base. One of the first steps an entrepreneurial enterprise could take is to develop its internal IP regulation. The author outlines only some practical matters (ownership of IP created within the employment context, a policy of rewarding employees’ creativity, and strategies to manage IP).

On account of the nature of legal entities, it is evident that a legal person cannot create any knowledge on its own. Therefore, a legal person has to establish a mechanism for control over the knowledge generated by its employees. This is especially important for Estonian entrepreneurs since the existing legal framework is inconsistent and insufficient.⁵³ For instance, § 12 (2) of the Patents Act⁵⁴ provides that “[i]f an invention is created in the performance of contractual obligations or duties of employment, the right to apply for a patent and to become the proprietor of the patent is vested in the author or other person pursuant to the contract or employment contract”.⁵⁵ However, pursuant to § 14 (2) of the Industrial Design Protection Act⁵⁶, “[t]he right to apply for the registration and ownership of an industrial design created in the performance of duties of employment or contractual obligations is vested in the employer or the customer, unless the duties of employment or the contract prescribe otherwise”. In practical terms, this means that if a person during an employment period or in the course of fulfilment of contractual obligations creates an invention and a design and IP issues are not *expressis verbis* agreed upon, then the right to apply for the registration of the design would belong to the employer or the customer and the right to apply for a patent would be vested in the inventor. The author of this article is unaware of conceptual considerations that explain why the ownership presumption is regulated differently in the cases of patents and designs.

Difficulties could arise also in relation to copyrights. Subsection 32 (1) of the Copyright Act⁵⁷ sets out a general rule, under which “[t]he author of a work created under an employment contract or in the public service in the execution of his or her direct duties shall enjoy copyright in the work but the economic rights of the author to use the work for the purpose and to the extent prescribed by the duties shall be transferred to the employer unless otherwise prescribed by contract”. Still, it is sometimes important for an employer to have a licence covering the author’s moral rights as well. For example, when an employee creates a logo, the economic rights shall be transferred automatically to the employer. However, the author’s consent is needed for change to the logo since, pursuant to § 12 (1) of the Copyright Act, the right of the integrity of the work and of supplementation of the work are moral rights that are not automatically transferred to the employer. In addition to problems related to moral rights, it is necessary that employment contracts are specific enough to define the direct duties of an employee. The reason is that the economic rights of an author are transferred to an employer only in respect of works created in the execution of the employee’s direct duties.

In summary, all of the potential problems described here that relate to the ownership of IP and could face entrepreneurs can be alleviated through the adoption of internal IP regulation. However, the author is somewhat confused when confronted with the present situation. At the moment, we have more than 70,000 enterprises in Estonia, all of which must consider the issue of IP ownership. The business reality is that a company in

⁵⁰ Green Paper. The European Research Area: New Perspectives – COM(2007) 161, 4.04.2007, p. 7.

⁵¹ E. R. Peterson (Note 8), p. 116.

⁵² B. Andersen (Note 11), p. 417.

⁵³ A very good analysis in respect of legal status of inventions created within employment or contractual relationships in Estonia is provided by J. Ostrat. See J. Ostrat. Töösuhtes või muu lepingu täitmisel tehtud leiutise õigusliku reguleerimise probleemide. Kas lepinguvabadus või eraldi seadus? (Problems in the Legal Regulation of an Employment-Relationship Invention. Freedom of Contract or a Separate Law?). – Juridica 2007/3, pp. 189–198 (in Estonian).

⁵⁴ Patendiseadus. Entered into force on 23.05.1994. – RT I 1994, 25, 406; 2007, 13, 69 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

⁵⁵ Subsection 11 (2) of the Utility Models Act provides similarly: “[i]f an invention is created in the performance of contractual obligations or duties of employment, the right to apply for the registration of a utility model and to become the owner of the utility model is vested in the author or another person pursuant to the contract or employment contract”.

⁵⁶ Tööstusdisaini kaitse seadus. Entered into force on 11.01.1998. – RT I 1997, 87, 1466; 2007, 13, 69 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

⁵⁷ Autoriõiguse seadus. Entered into force on 12.12.1992. – RT 1992, 49, 615; 2007, 13, 69 (in Estonian). Unofficial translation available at <http://www.legaltext.ee> (13.04.2008).

need of, say, a logo contacts some enterprise or individual and commissions creation of the logo. After the work has been done and approved by the customer, the latter pays the sum of money agreed upon. In another scenario, an employee generates new knowledge that could be packaged in the form of IP (e.g., a patent or design) in the course of employment and gets rewarded. The cases described could be regarded as involving normal business practice. Still, serious problems arise if IP issues are not agreed upon in detail. The Estonian legal environment requires entrepreneurs and other individuals to conclude special IP contracts, adopt internal regulations, etc. The author believes that it is not always necessary to change business practices and raise awareness among more than 70,000 Estonian enterprises; it would be more appropriate to make the Estonian legal environment more business- and innovation-friendly by providing, for instance, that in certain cases IP rights are assigned and conclusion of licence agreements is presumed automatically.

In order to leverage human capital, it is essential to establish an appropriate employee incentive system. The aim of incentives is to reward employees who contribute to generation of wealth. The development of the incentive system within a knowledge-based economy is a complicated challenge from both the legal and the economic standpoint — one that entrepreneurs have to face. Legal acts provide a general framework that needs to be taken into account in the design of economic incentives. Subsection 13 (8) of the Patents Act entitles an inventor to the following proprietary right: “An author has the right to receive fair proceeds from the profit received from the invention.”⁵⁸ A key issue for both employer and employee is how to interpret the concept of fair proceeds. The mere creation of IP (e.g., a patentable invention) should not necessarily be rewarded. It has been asserted that “technology by itself has no inherent value; that value only arises when it is commercialised through a business model”.⁵⁹ It is also necessary to bear in mind that a marketable product could be protected by many intellectual property rights (patents, design rights, trademarks, copyrights, etc.). Consequently, it is a quite complicated business to assess the value of a single protected invention. In addition, an entrepreneur might invest in many projects and find that only a few of them generate any returns. To sum up, the determination of what constitutes fair proceeds can only be based on economic analysis. Therefore, the legal framework has to be flexible and provide an employer and employee with considerable amount of freedom in determining their relations.

The success of a company depends a great deal on its business strategy. Best practice would be to incorporate an IP strategy into the general business strategy of each enterprise. An IP strategy should include guidelines on choosing an appropriate form of protection. For instance, after the creation of a patentable innovative solution, an entrepreneur faces three options: 1) to patent the invention or apply for a utility model, 2) to make the invention public, and 3) to keep the invention secret.

For numerous reasons, applying for a patent or a utility model is not always the best option. In order for one to patent an invention or apply for a utility model, the invention must be disclosed. This means that everyone can become aware of it. Since patent and utility model protection is territorially bounded and has time limits, it is possible to exploit the invention after the patent or utility model has expired or in jurisdictions where protection was not sought. Patenting is a costly procedure, and granting of a patent does not guarantee income. Even if the patent once issued is not invalidated for failure to comply with patentability criteria (concerning novelty, the inventive step, and industrial application) in a legal dispute, this does not mean that the patent is going to generate returns. A large proportion of patents do not yield any income. As a consequence of the lower costs, applying for utility model registration could be a good alternative to patenting. It is also necessary to consider that a single product could incorporate many patented inventions and other IPRs (e.g., designs, copyrights, and trade secrets). In these circumstances, it would be advisable to protect the core components or technology of the product rather than all possible features.⁶⁰ A decision to seek a patent or apply for a utility model should depend on the business model of the relevant enterprise.

Decision not to apply for a patent or utility model leads to another dilemma: to make the essence of the invention public or keep it secret. Both options have their advantages and disadvantages. The defensive publishing of the invention prevents someone else patenting it⁶¹ and as a result excluding others from using the invention. A company can disclose the invention itself or use someone else's services.⁶² However, after publication, the invention enters the public domain and no-one has control over it.

⁵⁸ Subsection 12 (8) of the Utility Models Act provides the same principle: “[a]n author has the right to receive fair proceeds from the profit received from the utility model”.

⁵⁹ H. W. Chesbrough (Note 25), p. 156.

⁶⁰ Trade secrets could be considered very useful tools to supplement patent and utility model protection. For instance, production of a product usually requires extra knowledge than the information which can be obtained from patent databases. In case this information is kept secret, the patent expiration does not necessarily mean that everyone can manufacture the product. They still need additional know-how.

⁶¹ In order to patent an invention, it must be new, involve an inventive step and be industrially applicable. Due to the publication, an invention loses its novelty.

⁶² For instance, IP.com offers a wide range of services including Prior Art Database as an outlet for publishing and searching technical disclosures. Further information available at <http://www.ip.com/> (18.04.2008).

A firm might prefer to keep the invention secret. As stated above, SMEs often protect their knowledge as trade secrets. On the one hand, this form of protection does not require following a formal registration procedure, filing of any applications, payment of a registration fees, etc., but, on the other hand, there are many complicated problems related to the protection of trade secrets. In order to have an effective protection strategy, entrepreneurs must clearly define⁶³ and list their trade secrets. The list should not be closed. It is recommendable to regulate who owns trade secrets developed by an employee. There is one additional practical matter that needs to be considered. Even if a company treats an invention as a trade secret, it is possible for another firm to create the same invention independently and patent it. In this scenario, the concept of prior user's right guarantees that the former company may continue to use the invention. Prior user's right is a statutory non-exclusive licence.⁶⁴ Subsection 17 (1) of the Patents Act describes the prior user's right as follows: "A person who, prior to the filing of a patent application for an invention by another person, has, in good faith and independently of the applicant, used the same invention for industrial application in the Republic of Estonia, may continue to use the invention retaining the same general nature of application".⁶⁵ Still, in order to rely on the concept of prior user's right, one must prove that one has that right. Therefore, a company's internal IP regulation should include well-specified procedures (e.g., files containing trade secrets could be signed digitally) to ensure the right of prior use for the firm even if the firm's trade secret becomes patented by someone else.

5. Conclusions

Because of the transformation into a knowledge-based economy, intellectual property has become an integrated component of the innovation process. Consequently, the IP system has to be constructed with the aim of enhancing innovation. In order for one to understand the contemporary concept of intellectual property fully, it is not sufficient to conceptualise IP either as an economic asset or as legal rights. The two aspects have to be integrated. In analysis of the essence of IP, it can be said that, despite the fact that the utilisation of knowledge takes place in business settings, the control over it is established within the legal system.

The framework conditions for innovation are essentially unique in every country, and fostering innovation requires tailor-made solutions. For instance, an important issue to be considered is the profile of the entrepreneurs. The majority of Estonian enterprises are small SMEs, which influences their capabilities to create, manage, and exploit IP. In order to be successful, small companies should adopt an Open Innovation model, which allows extraction of value from their knowledge without creation of an entire value chain on their own.

The author suggests that utility models could be very useful IP tools for SMEs, for a variety of reasons. The role of utility models is not limited to protecting incremental inventions. Positive features of utility models (e.g., lower inventive step requirement burden, affordable registration fees, and efficient protection) could lead to wide acceptance of this IP tool by entrepreneurs. All of this would create a good environment to enhance IP culture among Estonian enterprises. After development of capabilities to manage utility models, it would be easier to realise the potential of the patent system. Therefore, the author proposes analysis of the existing regulation concerning utility models and the practical implementation thereof, for identification and tackling of potential problems. It would be advisable to develop mechanisms encouraging and supporting the use of utility models. The author would also welcome substantial harmonisation of regulations concerning utility models at the EU level, to provide SMEs with a suitable IP tool to protect the results of innovation in many EU countries.

The theoretical literature and empirical surveys confirm that small firms usually prefer trade secrets to protect their knowledge base. Therefore, the author suggests critical review of the existing legal mechanisms for protection of trade secrets in economies such as that of Estonia, which consist largely of SMEs. The author is of the opinion that, because of presumption of high strategic relevance of trade secret protection to Estonian entrepreneurs, regulations on trade secrecy could be more detailed in Estonian legal acts. Even adoption of a special legal act (in such a form as an act on trade secrets) should be considered. The scope of information protected as trade secrets need not be necessarily extended. The main issue is, rather, to specify protection criteria, the legal status of trade secrets developed by an employee, procedural issues (e.g., the burden of proof), etc.

The success of an innovation does not depend solely on actions taken at the national or regional level. There is much that entrepreneurs could do. For instance, they could adopt internal IP regulations to address relevant issues such as ownership of IP created within the employment context, a policy to reward employees' creativity, and strategies for managing IP.

⁶³ In case trade secrets are not defined it is very complicated to prove that someone has misused them. See CCSCd, 16 November 2005, in matter 3-2-1-115-05. – RT III 2005, 40, 400 (in Estonian).

⁶⁴ It is still necessary to bear in mind that the concept of prior user's right might differ in different jurisdictions.

⁶⁵ Subsection 16 (1) of the Utility Models Act provides the same principle: "A person who, prior to the filing of a registration application for an invention by another person, has, in good faith and independently of the person who files the registration application, used the same invention for industrial application in the Republic of Estonia, may continue to use the invention retaining the same general nature of application".



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The Estonian Universal Enforcement Procedure^{*1} and the Bailiff as the Taker of Procedural Decisions

1. Introduction

After regaining independence, Estonia has experimented with compulsory execution by both the executive power and judicial power.^{*2} The enforcement procedure reform of 2001 decided in favour of freelance bailiffs and the system has proved to be effective — with the number of closed files doubling one year after the reform.^{*3}

The purpose of this article is to analyse how to classify enforcement proceedings in the Estonian legal system and what position and competence the legislature has given to the bailiff. The analysis also has relevance in the European context, as the European enforcement instrument introduced from 1 March 2002^{*4} as a reaction to “mobile debtors” has not, because of the great variety of enforcement procedure regulations in the Member States, made things much easier for creditors, and this is why attempts are being made to harmonise the legal orders of the Member States and identify the most effective procedure.^{*5}

The Estonian law of enforcement procedure is difficult to classify into a particular branch of law: it is separated formally from other areas of law by a specific law, and organisationally by a separate enforcement body — the freelance bailiff. As the matter of jurisdiction in disputes regarding enforcement proceedings has caused several

¹ The author of the article considers only singular execution, i.e., enforcement proceedings, not bankruptcy proceedings.

² In 1994–1997 the Ministry of Justice had an Enforcement Department; the enforcement bureaux under it enforced civil claims. In 1997, these enforcement bureaux were replaced by the enforcement departments of courts, i.e., bailiffs became a part of judicial power. For details see J. Ots. *Tsiviilitäitemenetluse ja kohtutäituri institutsiooni areng pärast Eesti Vabariigi taastamist. Magistritöö* (Development of Civil Enforcement Proceedings and the Institution of the Bailiff after Restoration of the Republic of Estonia. Master’s Thesis). Tartu 2002, p. 21–22, 91 ff. (in Estonian).

³ Ministry of Justice statistics, published in the conference compilation. *Kohtutäiturid ja riigivõimu jagamine* (Bailiffs and Delegation of Public Power), 1–2 March 2002, Tallinn (in Estonian).

⁴ Council Regulation (EC) No. 44/2001, 22 December 2000, on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. – OJ L 12, 16.1.2001, p. 1.

⁵ For details see, e.g., M. Andenas, B. Hess, P. Oberhammer. *Enforcement Agency Practice in Europe*. London: British Institute of International and Comparative Law 2005.

disputes in Estonia which have reached the Supreme Court, the first part of the article discusses the difficulty of classification and the reasons for the difficulty. The author also tries to answer the question of whether different procedural rules and principles are actually necessary for the enforcement of private and public claims.

Not only the issue of the procedural rules, but also the status of the bailiff, is often unclear to the parties to a proceeding. The bailiff is regarded as a representative of the claimant, similar to a trustee in bankruptcy, or a state official, depending on whether the claim being enforced is a private or public claim. According to § 2 (2) of the Bailiffs Act, a bailiff is neither an undertaking nor a state official; § 9 (1) of the Code of Enforcement Procedure requires a bailiff to remove himself or herself from enforcement proceedings if he or she is also the representative of the claimant. The term “freelance” raises the question of whether the profession of a bailiff should be accessible to everybody and whether there should be free competition between bailiffs within the meaning of the directive on services in the internal market.^{*6} In the second half of the article the author analyses the position of a bailiff in the structure of the authority of the state, and a bailiff’s resulting competence.

2. Enforcement proceedings as civil enforcement?

2.1. Estonian universal enforcement procedure

In Estonia, enforcement proceedings are often called “civil enforcement proceedings”, as if they are only applied to private law relationships. This is how it is in many European countries; discussions on the harmonisation of European enforcement procedures usually concern only enforcement instruments arising from civil and commercial relationships and leave out the regulation of public law claims as an area closely related to the exercise of the authority of the state.^{*7}

If we view only the enforcement of private persons’ claims in enforcement proceedings, then the classification of enforcement proceedings as an area of private law is somewhat justified. Already at the beginning of the last century, the German jurist Friedrich Stein drew attention to the fact that enforcement proceedings begin and end in private law.^{*8} It should be noted though that in Germany, enforcement proceedings are, first and foremost, seen as a follow-up to civil procedure, which enforces only private claims, and many legal theorists have reasoned the private law classification of enforcement proceedings with the theory of interest: proceedings are conducted in the claimant’s interests, and the relationship between the claimant and debtor is that of two equal parties.^{*9}

The Estonian Code of Enforcement Procedure^{*10} (hereinafter: CEP) recognises various enforcement instruments arising from civil relationships: court decisions and rulings in civil matters, decisions of foreign courts in disputes between private individuals, decisions of extrajudicial bodies, notarised mortgage contracts and pledge contracts of buildings, and notarised agreements concerning financial claims. The same executive body also executes completely different enforcement instruments under the same Code: fines imposed in misdemeanour proceedings, fines applied as criminal punishments, tax decisions, etc.^{*11} In the list of enforcement instruments provided in CEP § 2 (1), public law liabilities significantly outnumber instruments issued for the enforcement of private claims. The enforcement procedure statistics published on the Ministry of Justice’s website also indicate a large proportion of public law claims. As of the end of 2007, the total of 201,834 open enforcement files included 36,541 files concerning private claims.^{*12}

The Estonian enforcement procedure thus covers various other proceedings: not only civil proceedings, but also administrative, criminal, tax, misdemeanour and extrajudicial proceedings. This varied list of enforcement instruments shows that in Estonian law, enforcement proceedings are not only a follow-up to civil proceedings, but also a follow-up to criminal, administrative court, administrative, misdemeanour and tax proceedings, labour dispute settlement and other procedures. Since appeals against the acts of a bailiff fall under the general jurisdiction (CEP § 218 *ff.*), every compulsory execution may at some point, via the “filter” of enforcement proceedings, become a civil proceeding.

⁶ Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market. – OJ L 376, 27.12.2006, p. 36–68.

⁷ See, e.g., M. Andenas. National Paradigms of Civil Enforcement, p. 7. – M. Andenas, B. Hess, P. Oberhammer. Enforcement Agency Practice in Europe. London: British Institute of International and Comparative Law 2005.

⁸ F. Stein. Grundfragen der Zwangsvollstreckung, 1913, p. 6, referred in: G. Lüke. Bausteine des Zwangsvollstreckungsverfahrens. – Juristische Schulung 1996, p. 185.

⁹ E.g., E. Wieser. Grundzüge des Zivilprozeßrechts: mit Zwangsvollstreckungs- und Konkursrecht. Köln: Carl Heymanns Verlag 1986, p. 73.

¹⁰ Täitemenetluse seadustik. – RT I 2005, 27, 198; 2007, 25, 130 (in Estonian).

¹¹ For the list of enforcement proceedings see CEP § 2 (1).

¹² Enforcement procedure statistics published by the Ministry of Justice. Available at http://www.just.ee/orb.aw/class=file/action=preview/id=35506/aruandlus_2007_n%F5uete+j%E4rgi.pdf (8.05.2008) (in Estonian).

In addition to the above, under CEP § 2 (1) a bailiff also enforces rulings on the securing of an action, which are acts of civil procedure, as well as investigators' rulings for collection of information about the property of an accused, and requests substitution by detention of fines for misdemeanours and monetary fines and fines to the extent of assets, which have been imposed as criminal punishments — these may be regarded as acts of criminal procedure. In addition, under the Immovables Expropriation Act^{*13}, a bailiff has the duty to participate in determining the price of an immovable.

Based on the above, the Estonian enforcement procedure can be regarded as a universal procedure, in which a bailiff performs acts in the course of which the bailiff may and can exercise duress and which are not in the competence of any other body. The author of this article considers that this universal procedure certainly belongs to public law and is positioned somewhere on the border between procedural law and administrative law.

The use of common procedural rules and a single central procedural body avoids a “race” for the debtor's assets by executive bodies acting under parallel compulsory execution proceedings, and renders the proceedings clearer and simpler for the debtor, who only has to communicate with one bailiff who is conducting the proceedings — this is certainly a strength of the Estonian regulation when compared to a multiplicity of compulsory execution proceedings. Simplicity and clarity, however, cannot serve as a goal on its own, and it is appropriate to ask at this point whether the procedure should for any reason be different for private and public law claims.

2.2. Procedural principles

When studying the universal procedure applicable in Estonia, one may ask whether the procedure rules and principles can really be the same for instruments produced as a result of a dispute between equal parties, on one hand, and for the enforcement of the state's obligations or criminal punishments, on the other.

The Code of Enforcement Procedure provides for a different procedure only for the enforcement of monetary fines and fines to the extent of assets which have been imposed in misdemeanour and criminal proceedings (CEP § 198 *ff.*). Firstly, these are the only types of claim for which the legislature has provided for *gradus executionis* for making claims against the debtor's assets, i.e. a claim for payment is first made on money, securities and claims, followed by other movables, and, in the last order, immovables, while preference is given to the debtor's separate property over the joint property of spouses. Secondly, these enforcement instruments allow for substituting the claim on the debtor's assets by detention, i.e. making a claim on the debtor's person. The third major difference is the limitation period for enforcement depending on the gravity of the misdemeanour: 18 months, three or five years, during which the proceedings must result in the collection of a fine or substitution of the punishment. The procedure for enforcement of other public claims, such as local taxes, is exactly the same as for private claims.

In comparison, in Germany the compulsory execution of public claims is subject to specific laws for each type of claim and is performed by different bodies. The enforcement of administrative acts is governed by *Verwaltungs-Vollstreckungsgesetz*^{*14}, tax decisions are subject to *Abgabenordnung*^{*15}, and fines in criminal matters are governed by *Strafprozeßordnung*^{*16} and *Justizbeitreibungsordnung*.^{*17} Public law claims are justified to be enforced by the entitled person, i.e. a relevant state agency, while the proceedings are not traditionally classified as enforcement proceedings; the compulsory execution of tax decisions and criminal fines is classified as a part of tax proceedings and criminal proceedings, respectively.^{*18} However, if we compare the procedures and principles of various enforcement proceedings, the procedure is essentially the same for all types of claim: the debtor is first given a deadline for voluntary compliance, after which a claim is made on the debtor's assets; the principle of proportionality applies, etc. In the Netherlands, enforcement actions are divided between different bodies (bailiff, court, notary), but compulsory enforcement is governed by a single law (*Rechtsvordering*).^{*19}

¹³ Kinnisasja sundvõõrandamise seadus. – RT I 1995, 59, 1006; 2007, 24, 128 (in Estonian). A bailiff's participation in the appraisal is regulated by § 16 of the Act.

¹⁴ Verwaltungs-Vollstreckungsgesetz. Passed 27.04.1953, last amended 17.12.1997 I 3039. – BGBl I 157. Available also at <http://bundesrecht.juris.de/vwvg/index.html> (8.05.2008).

¹⁵ Abgabenordnung. Passed 16.03.1976, last amended 23.10.2008 I 2026. – BGBl I 3198. Available also at http://bundesrecht.juris.de/bundesrecht/ao_1977/gesamt.pdf (8.05.2008).

¹⁶ Strafprozeßordnung. Passed 12.09.1950, last amended 31.10.2008 I 2149. – BGBl I 306. Available also at <http://bundesrecht.juris.de/bundesrecht/stpo/gesamt.pdf> (8.05.2008).

¹⁷ Justizbeitreibungsordnung. Passed 11.03.1937, last amended 17.12.2006 I 3171. – BGBl III 365-1. Available also at <http://bundesrecht.juris.de/jbeitro/BJNR002980937.html> (8.05.2008).

¹⁸ H. Hofmann, J. Gerke. Allgemeines Verwaltungsrecht. Stuttgart: Kohlhammer Deutscher Gemeindeverlag 2002, p. 444 *ff.*

¹⁹ T. Jongbloed. National Reports. The Netherlands, p. 208. – M. Andenas, B. Hess, P. Oberhammer. Enforcement Agency Practice in Europe. London: British Institute of International and Comparative Law 2005.

This means that the legislature has not seen any need for different procedural principles when dividing compulsory execution proceedings between different branches of law and different enforcement bodies. This is understandable because in both cases claims are based on instruments sanctioned by the state. Important from the debtor's viewpoint are the clarity and indisputability of the claim and its foundation on a legally certain source. Once a claim has been accepted, the means of enforcement are, in any case, firstly influencing the debtor by an enforcement body, and if this fails, then compulsory execution. A meaningful question in this context is: which public instruments should be or should not be recognised as enforcement instruments? However, this should be a legal policy decision, which is beyond the scope of this article. It is important to note that there is no practical need for different procedure rules. Special provisions, which are necessary for some types of claims, e.g., the Estonian possibility of substituting fines by detention in criminal matters, can always be added to the regulation.

2.3. The issue of jurisdiction

The classification of enforcement proceedings as an area of law has caused disputes in Estonia as to the jurisdiction of appeals against a bailiff's acts. Already in 1998, when bailiffs were officers of the courts, the Supreme Court had to stress that appeals in enforcement proceedings were subject to settlement according to civil procedure, because, despite the provision of the Code of Enforcement Procedure, the court of appeal considered the administrative court to be the competent court.^{*20} On 15 March 2002, the Special Panel of the Supreme Court had to adopt a position and found that courts of general jurisdiction are the competent courts.^{*21} The disagreements of the court on this issue were due to the ambiguousness of legal regulation, on the one hand, and different interpretations of the activity of bailiffs, on the other. The Supreme Court once again had to draw attention to the general jurisdiction of appeals against bailiffs, on 28 March 2002.^{*22}

Currently, disputes arising from enforcement proceedings are singularly in the competence of courts of general jurisdiction according to § 218 ff. of the CEP, which entered into force in 2006. General jurisdiction seems to refer to private disputes between equal parties.

In countries where compulsory execution is divided between different enforcement bodies, the legal remedies arise from the general regulation of the specific area, i.e. disputes arising from the enforcement of public law claims are generally in the jurisdiction of the administrative court. This is the case, for example, in Switzerland, where the entire enforcement procedure is considered to be an administrative procedure because of its predominantly law-making nature, characteristic of the administrative procedure, although it is usually private positions that are confronted in enforcement proceedings.^{*23}

The extension of general jurisdiction to all enforcement proceedings in Estonia may be regarded as tradition, because when bailiffs were state officials, they also enforced public claims, and as court officials, they were subject to the supervision of courts of general jurisdiction. On the other hand, there is the principle of efficiency, according to which disputes arising from the same procedure rules should not be settled by different courts. From the debtor's viewpoint, there could be a difference in the principle of competition between the parties, which is characteristic of the civil court, while in administrative court proceedings, the court would also be obliged to collect evidence on its own initiative. Appeals against the acts of a bailiff are reviewed in Estonia on petition, according to § 475 of the Code of Civil Procedure^{*24}, in which the court is not tied to the requests and assessments of the parties to the proceedings, and the court may also demand additional evidence or collect evidence on its own initiative. In the event of a substantive dispute, e.g., the establishment of ownership relations, decision on the validity of an auction, declaration of compulsory execution as inadmissible, etc., an action is prescribed, in which case the parties to the proceedings should reason their positions and present relevant evidence regardless of jurisdiction. Therefore, it cannot be said that the debtor's position is less protected by a single jurisdiction than it is by varying jurisdictions, although because of the confrontation of an individual with the authority of the state in enforcement proceedings, the author of this article believes that the jurisdiction of the administrative court would be a more logical choice. In any case, one may take the view that in the universal enforcement procedure, a single jurisdiction ensures the uniform application of law for the parties to the proceedings, as well as for the courts, better than the division of disputes between various courts.

²⁰ CCSCr 4 March 1998, 3-2-1-25-98. – RT III 1998, 9, 97 (in Estonian).

²¹ Ruling of the Special Panel of the Supreme Court, 15 March 2002, 3-3-4-3-02. Available at <http://www.riigikohus.ee/?id=11&tekst=RK/3-3-4-3-02> (8.05.2008) (in Estonian).

²² CCSCr 28 March 2002, 3-2-1-36-02. – RT III 2002, 12, 133 (in Estonian).

²³ Y. Iqbal. SchKG und Verfassung – untersteht auch die Zwangsvollstreckung dem Grundrechtsschutz? Zürich: Schulthess Juristische Medien AG 2005, p. 47.

²⁴ Tsiviilkohtumenetluse seadustik. – RT I 2005, 26, 197; 2007, 16, 77; RT III 2008, 16, 105 (in Estonian).

3. Legal position of a bailiff

3.1. The bailiff in the structure of the authority of the state

The institute of a freelance bailiff, established by the Bailiffs Act (hereinafter: BA) which entered into force on 1 March 2001, is similar chiefly to the French, Belgian, and Slovak systems, in which the bailiff is also a freelancer. BA § 2 (1) defines a bailiff as an independent person who holds an office in public law. Subsection 2 of the same section designates a bailiff's office as a liberal profession, stressing that a bailiff is neither an undertaking nor a state official. An Estonian bailiff is characterised by appointment by the Minister of Justice, *numerus clausus* of bailiffs' offices, restrictions related to office, and establishment of the rates of bailiff's fees by law. A bailiff is liable for his or her activities under BA § 6 (3) as a public authority on the basis of the law governing the procedure and extent of state liability.

It is appropriate to note in the European Union context that the status of a bailiff is defined in Estonia in the same way as a notary's status — as a liberal profession and a public authority. If the EU Commissioner for competition proposes to abolish the *numerus clausus* of the number of notaries²⁵, the same should essentially apply to bailiffs. We may argue over whether the use of the national coat of arms in the event of a notary refers to the exercise of the authority of the state or whether impartial and independent legal advice is possible under free market conditions, while in the event of bailiffs the exercise of the power of the state is much better manifested, and leaving the state's power of duress up to public competition seems unreasonable, even without a lengthy justification. Due to the above, restrictions on access to the profession and on the professional activities of a freelance bailiff are certainly justified.

In countries where enforcement proceedings are conducted by bodies of the executive power (e.g., Switzerland) or by bailiffs as officers of a court (e.g., Germany), the status of a bailiff is defined by the organisation to which the bailiff belongs — the bailiff is an officer of the executive or judicial power. Classifying a freelance bailiff as a public authority raises the question of which function of the authority of the state the bailiff indeed has. This question seems easiest to answer by way of exclusion. A bailiff does not create new law, neither does he or she take decisions toward settling disputes between parties; hence a bailiff has no legislative or judicial function. Taavi Annus has called the duty delegated to bailiffs as the state's executive function.²⁶ The executive function of a bailiff consists in the enforcement of single acts — administrative acts, court decisions, etc. — adopted on the basis of law. The Tallinn City Court has found that a bailiff performs the state's administrative function, which is why a bailiff's fee is a monetary obligation in the area of public law.²⁷ According to Kalle Merusk's models of delegation of public functions, a freelance bailiff has become the performer of administration as a part of indirect public administration, carrying out duties within the competence of public authority in his or her name.²⁸ The fact alone that the conduct of enforcement proceedings is covered by the right to recourse to the courts, as provided in § 15 of the Constitution of the Republic of Estonia²⁹, which the state has to guarantee, refers to the competence of public authority.

If a bailiff is defined as a performer of administration in Estonia, then considering the peculiarities of various types of claims, a bailiff still has to attempt to pursue a double role: being the impartial third between two private interests in the event of private claims, and acting as the tool of the state in the event of public claims.

The access of bailiffs to state registers is justified if they are regarded as public authorities, and so is the duty of private individuals to supply a bailiff with the information necessary for the proceedings (CEP §§ 22, 26) and criminal punishment for supplying a bailiff with incorrect information (§ 281 of the Penal Code). A bailiff's limited access to information about debtors' assets has been pointed out as a factor hampering the efficiency of proceedings in the case of, e.g., English and Welsh bailiffs, who may or may not be state officials³⁰, and in the case of French freelance bailiffs.³¹

²⁵ A. Oja, T. Arnover. Volinik surub notareid ja panku vabaturule (Commissioner Pushes Notaries and Banks to Open Market). – Äripäev, 21.06.2007, pp. 1, 4–5 (in Estonian).

²⁶ T. Annus. Riigi funktsioonide delegerimine eraõiguslikele isikutele kohtutäiturite näitel (Delegation of State Functions to Persons in Private Law). – Juridica 2002/4, p. 225 (in Estonian).

²⁷ Ruling of the Tallinn City Court, 9 October 2003, 2/33-3238/03 (in Estonian).

²⁸ K. Merusk. Avalike ülesannete eraõiguslikele isikutele üleandmise piirid (Limitations to the Transfer of Public Functions to Persons in Private Law). – Juridica 2000/8, p. 505 (in Estonian).

²⁹ M. Ernits. Kommentaarid EV põhiseaduse paragrahvile 15 (Commentaries on § 15 of the Constitution of the Republic of Estonia). Eesti Vabariigi põhiseadus: kommenteeritud väljaanne (Constitution of the Republic of Estonia: Commented Edition). Tallinn: Juura, Õigusteabe AS 2002, p. 138 (in Estonian).

³⁰ M. Andenas. National Reports. England and Wales, pp. 151–152. – M. Andenas, B. Hess, P. Oberhammer. Enforcement Agency Practice in Europe. London: British Institute of International and Comparative Law 2005.

³¹ M.-L. Niboyet, S. Lacssagne. National Reports. France, pp. 165–166. – M. Andenas, B. Hess, P. Oberhammer. Enforcement Agency Practice in Europe. London: British Institute of International and Comparative Law 2005.

3.2. Delimitation of the competence of bailiffs and courts

In the Estonian system, a bailiff is not the only one who settles enforcement cases, because certain acts can be decided only by a court; disputes arising from the proceedings and appeals against a bailiff's acts are also in the jurisdiction of the courts. The division of tasks between bailiffs and courts may be based on various principles, such as leaving the acts less impinging on a debtor's fundamental rights in the bailiff's domain, and letting the courts control those acts which impinge on fundamental rights more strongly. In the following, the author will look at how the Estonian legislature has divided these tasks.

According to the CEP, the bailiff's competence covers mainly routine or technical acts such as informing a debtor of the procedure, explaining to the parties their rights, seizure of property and entry of notations concerning prohibition in registers, receipt and delivery to the claimant of money from the debtor or of the sales proceeds of property, keeping record of receipts, etc. On the other hand, a bailiff also takes evaluative decisions on some issues. The most important decisions that a bailiff is competent to take in proceedings are: determination of the order of seizure of property (CEP § 53 (3)), appraisal of seized property (CEP § 74 (4), (5)), determination of ownership in certain cases (CEP § 64 (4), § 77 (2), § 181 (2)), determination of the method of sale of property outside auction (CEP § 101), identification of the debtor's dependants and economic status (CEP § 132 (2), § 133 (2)), preparation of a distribution plan for received money (CEP §§ 106–108, 174–177), and decision on the necessity of suspension of proceedings (CEP § 46 (2)).

Leaving these issues up to the bailiff is not the only option that the legislature has. For example, the Slovakian provisions on the appraisal of property prescribe expert appraisal of property which is to be put up for auction.³² In Estonia, in the absence of an agreement between the debtor and bailiff, it is the bailiff who usually determines the price under CEP § 74 (4) and (5), based on the market value and any rights encumbering the property. As regards property whose market value is relatively easy to determine, such as dwellings, it is probably expedient not to involve an expert, while in more complicated cases, a bailiff himself or herself should be able to decide that expert appraisal is necessary. In Germany, bailiffs are competent to appraise movables, unless the debtor or claimant requests the court to appoint an expert (ZPO § 813); for immovables, the court appoints an appraiser where necessary (ZVG³³ § 74a (5)). In Germany, filing a claim against assets is in the competence of the court, specifically the assistant judge organising the proceedings; in Estonia, the court's involvement is necessary only upon the appointment of a compulsory administrator for an immovable.

There are not many issues in CEP which should certainly be settled by a court in the course of enforcement proceedings. The courts are competent to grant a search warrant (CEP § 28), obtain from the debtor a sworn list of property (CEP § 61), grant permission for the seizure of a pet (CEP § 67 (2)), order an immovable to compulsory administration (CEP § 162), recover a debtor's transactions which damage the creditors' interests (CEP § 187 *ff.*), and substitute a fine or a fine to the extent of assets by detention (CEP §§ 201, 206). As regards other acts, the court's intervention depends on the request of the parties to the proceedings or their mutual dispute: removal of a bailiff (CEP § 9), suspension of proceedings (CEP § 45, § 109 (2)), as well as actions for declaring an auction invalid (CEP § 223), settlement of ownership disputes (CEP § 73 (2)), division of joint property (CEP § 14 (2)) or declaration of compulsory enforcement to be inadmissible (CEP §§ 220–222) and appeals against a bailiff's other acts according to CEP § 218. In the latter issues, the bailiff takes an initial decision and referring to the court is usually the response of a party to the proceedings if the party is not satisfied with the bailiff's solution. If none of the parties to the proceedings contests an act, a "wrong" or unfair solution may remain in force.

It is difficult to find a common denominator for the issues which are unconditionally placed under the control of the courts. Granting a search warrant and ordering the detention of the debtor are clearly limitations of the debtor's fundamental rights; seizure of a pet relates to the debtor's emotional ties to the pet. While in Germany, it is the court (assistant judge) which eventually decides on filing a claim against immovables or claims, in Estonia these issues are in the sole competence of a bailiff, the only exception being the little-used compulsory administration of an immovable. Compulsory administration does not impinge on the debtor's ownership rights as strongly as compulsory sale, and the court's role can be considered organisational. Swearing to the correctness of the debtor's list of property has to ensure the authoritativeness of the act and stress to the debtor his or her liability for the submission of incorrect information. The recovery of transactions is largely a legal assessment and the settlement of a legal dispute.

One of the common characteristics in the issue of where the court's involvement is mandatory is the infrequent occurrence of the aforementioned acts and hence their rather exceptional nature in daily enforcement practices. Using the routine and more frequently used acts and measures of enforcement proceedings is up to the bailiff. Such a solution is certainly justified with regard to the efficiency of proceedings, as it allows for

³² B. Schönfelder. Courts, credit and debt collection in post-communist Slovakia. *Economic Annals* No. 167, October 2005–December 2005, p. 28. Available at <http://www.doiserbia.nbs.bg.ac.yu/img/DOI/0013-3264/2005/0013-32640567007S.pdf> (27.04.2007).

³³ *Zwangsversteigerungsgesetz*. Adopted on 24.03.1897, last amended on 23.11.2007. – BGBl I 2614. Available at <http://bundesrecht.juris.de/bundesrecht/zvg/gesamt.pdf> (8.05.2008).

quick proceedings, but may be problematic in the context of the protection of fundamental rights where the debtor is without legal knowledge and considers referring to a court to be complicated and expensive, or is otherwise psychologically ruined because of the events. This is why a bailiff's decisions must be procedurally ensured to be in line with the principles of impartiality, objectiveness and proportionality.

3.3. Bailiff's discretion

3.3.1. Existence of discretionary power

In order to preclude arbitrary action by a freelance bailiff where duress is exercised, the principle of formalisation of enforcement proceedings must be ensured; the Supreme Court has also drawn attention to it.^{*34} According to this principle, a bailiff does not settle substantive legal issues when conducting compulsory execution proceedings, but follows the enforcement instrument, and certain formal circumstances are required for both the commencement of proceedings and for the bailiff's acts. As enforcement proceedings mean the execution of a decision that has already been discussed and settled and hence the proceedings no longer entail a discussion of substantive issues, it seems inappropriate to speak about discretion and decision in this context.

However, the legislature has considered it expedient not to prescribe the exact rules of conduct in many provisions on enforcement proceedings, but to leave the appropriate solution up to the court or bailiff, thus making it possible to take into account the specific features of the case and achieve a fair solution. The right to decide and choose the suitable solution can be called discretion or discretionary power; these terms are mainly used in the context of administrative law.

As regards a bailiff's discretion, the Supreme Court, in decision No. 3-2-1-104-04, stated the view that when deciding on the suspension of proceedings, a bailiff has to consider, following the principle of formalisation, whether or not the appeal filed prevents the enforcement of the decision.^{*35} The Supreme Court thus links discretion to formalisation. The court apparently had in mind formalisation in deciding on the possibility of an offset which caused the dispute in this case, because in a number of issues where the bailiff's decision is required, the principle of formalisation is of no great help to a bailiff. In the conducting of proceedings, the application of formalisation is justified in the event of the question "whether", as the content of the enforcement instrument is not re-checked; while the formalisation of "how" would reduce the efficiency of proceedings.^{*36}

Namely, it is impossible to establish exhaustive rules of procedure for every possible situation without leaving any space for choice. For the event of unforeseeable and exceptional procedural acts resulting in disproportionately grave consequences for the debtor, it is reasonable for the legislature to provide for a bailiff's discretionary power and the obligation to refuse to perform an act or to conduct an act in a special manner in relevant circumstances. Similarly to the German regulation of enforcement proceedings, Estonian bailiffs essentially have the role resembling that of a German court in compulsory execution in certain cases. The question is whether the legislature has provided a bailiff with sufficient guidelines for deciding in order to ensure the proportionality of proceedings and protection of the fundamental rights of the parties to the proceedings?

The legislature has to define the limits and maximum extent of impingement on fundamental rights; a bailiff always has the freedom to impinge on rights to a lesser extent if that is justified considering the circumstances of the proceedings. A bailiff also has to consider that protection of the interests of one party to the proceedings is impingement of the rights of the other. A claimant's constitutional ownership right is, in this case, confronted with the debtor's ownership and fundamental social rights.

According to Merusk, discretion means the competence to freely assess the situation and take an appropriate decision.^{*37} According to § 4 of the Administrative Procedure Act, discretion is an authorisation granted by law to consider taking a decision or choose between different decisions, while taking into account the limits of authorisation, the purpose of discretion, general principles of justice, relevant facts and legitimate interests. In enforcement proceedings, such free assessment of the situation is thinkable upon the exercise of duress, for example, where a bailiff has to decide on the assets which according to CEP § 66 are not subject to seizure but remain at the debtor's disposal. It is therefore important to define the balance between formalisation and discretion in enforcement proceedings and the principles that a bailiff has to follow when exercising discretion, because absolute discretion is, of course, unthinkable.^{*38} The latter arises from § 3 (1) of the Constitution, which ties the entire exercise of the authority of the state to the Constitution itself and laws which are in conformity therewith. The classification of a bailiff as a public authority was already mentioned above.

³⁴ CCSCd 16 October 2002, 3-2-1-119-02. – RT III 2002, 27, 304 (in Estonian).

³⁵ CCSCd 8 October 2004, 3-2-1-104-04, item 11. – RT III 2004, 25, 277 (in Estonian).

³⁶ F. Baur, R. Stürner. *Zwangsvollstreckungs-, Konkurs- und Vergleichsrecht*. Heidelberg: C.F.Müller Verlag 1995, p. 88.

³⁷ K. Merusk. *Administratsiooni diskretsioon ja selle kohtulik kontroll* (Discretion of Administration and its Judicial Review). Tallinn: Juura, Õigusteabe AS 1997, p. 10 (in Estonian).

³⁸ *Ibid.*, p. 11.

Jellinek's approach to discretion as the furnishing of an undefined legal concept^{*39} makes it possible to describe a bailiff's activities under the CEP. As most other laws, the CEP cannot escape the use of undefined legal concepts. For example, in determining the order of seizure of assets according to CEP § 53 (3), a bailiff has to consider that the claimant's claim has to be granted in the fastest manner without damaging the debtor's legitimate interests. The content of "legitimate interests" has to be decided on a case-by-case basis.

The Supreme Court has noted that the legislature has to decide all issues relevant from the aspect of fundamental rights, and must not delegate such decisions to the executive power. The executive power may only elaborate on the restrictions established by law, but not impose additional restrictions.^{*40} Enforcement proceedings mainly impinge on the debtor's ownership rights, while the existence of non-seizable property impinges on the claimant's ownership right. The CEP does not authorise a bailiff to impose any restrictions of his or her own; the law defines non-seizable assets in detail (CEP § 66 — non-seizable assets; CEP §§ 131, 132 — income on which a claim for payment cannot be made). Anything not listed may be seized, subject to the prohibition on excessive seizure. In a bailiff's activities, discretion cannot mean a choice as to the objective of the proceedings, but only as to the means used, and even then subject to the measures prescribed by the legislature. Hence, we can speak about discretion in terms of expedience and efficiency.

The exercise of discretion may be divided into two: discretion of choice or the right to choose the most expedient outcome, and discretion of decision or a decision on whether or not to apply the legal consequence provided by law.^{*41} An example of the first is the order of seizure of property which a bailiff determines in the course of enforcement proceedings; discretion of decision is exercised when a bailiff has to decide on the need to suspend proceedings if an appeal is filed against the bailiff's acts.

Enforcement proceedings always entail a conflict of fundamental rights, the settlement of which is one of the legal limits to the exercise of discretion.^{*42} The bailiff has to consider the conflicting interests and take a decision without distorting the nature of any of the rights or freedoms being impinged on.

For a number of situations, the legislature has prescribed which fundamental right takes priority over another. For example, the debtor's right to a decent living and the aid of the state in the event of need are, as a rule, preferred to the requirement for the defence of the claimant's ownership, via the establishment of non-seizable assets and types of income. Certain items and income have to remain at the debtor's disposal even if this means the impossibility of meeting the claim or postponement of the final execution of the enforcement instrument into the distant future. However, as an exception to this rule, it is possible under CEP § 66 (2) to seize a debtor's necessary household effect if the item belongs to the claimant and a financial claim, which is ensured by ownership reservation, is being enforced concerning the same item. The legislature has not imposed a direct obligation on the claimant to support the debtor from the claimant's assets.

In certain cases, however, the choice is up to the bailiff, who has to exercise his or her discretion in line with the principle of proportionality and select which right to restrict in favour of what. For example, under CEP § 131 (2), a part of income which is usually not seized, may be seized in certain cases, considering the type of the claim, the amount of income and fairness, while the bailiff has to hear the debtor before taking the decision only if the bailiff has the possibility to do so. As regards compliance with the principle of proportionality, the Supreme Court has emphasised that when deciding on the manner of enforcing a claim, in addition to hearing the debtor, consideration should be given especially to the claimant's interests and the objective of efficiency of enforcement proceedings, and thus the expedience of the act has to be analysed.^{*43} These guidelines were given, however, to a court and not a bailiff. The Supreme Court has further found that discretion is necessary for ensuring the application of the principle of proportionality in proceedings. As a rule, a competent body has the duty to assess whether a person's interests are balanced with public interest, i.e. whether the restrictions on fundamental rights are proportional. The specific circumstances of the case have to be taken into account to assess the compliance of a decision with the principle of proportionality.^{*44}

³⁹ W. Jellinek. *Verwaltungsrecht*. Berlin, 1928, referred to in: K. Merusk (Note 37), p. 15.

⁴⁰ CRCSd 24 December 2002, 3-4-1-10-02. – RT III 2003, 2, 16 (in Estonian).

⁴¹ K. Merusk (Note 37), p. 25.

⁴² *Ibid.*, p. 31.

⁴³ CCSCr 22 December 2003, 3-2-1-147-03, item 12. Available at [\(http://www.nc.ee/?id=11&indeks=0,2,237,1397&tekst=RK/3-2-1-147-03\(8.05.2008\)\)](http://www.nc.ee/?id=11&indeks=0,2,237,1397&tekst=RK/3-2-1-147-03(8.05.2008)) (in Estonian).

⁴⁴ CRCSd 21 June 2004, 3-4-1-9-04, item 16. – RT III 2004, 20, 224 (in Estonian).

3.3.2. Discretionary errors

Maurer points out three types of errors in the exercise of discretion: exceeding the limits, non-use, and misuse of discretionary power.^{*45}

Exceeding the limits of discretionary power means that the decision is beyond the competence of the decision-maker. For example, a claimant may agree with the debtor that the claim will be paid in instalments according to a schedule. If a payment schedule is agreed between the debtor and bailiff without asking the claimant's opinion, the bailiff has taken a decision which is beyond his or her competence.

Non-use of discretionary power means that the possibility of taking various circumstances into account is not used. This is the case, for example, if a bailiff, at the claimant's request under CEP § 131 (2) seizes the entire parental benefit paid to the debtor without taking into account the special needs of the debtor's child and the existence or lack of other income of the debtor, and considers the claimant's request the only necessary prerequisite for seizing the parental benefit. Non-use of discretionary power also occurs if the bailiff is aware of all the debtor's assets, but instead of seizing these awaits the claimant's opinion as to which part of the debtor's assets the claimant wishes to be seized. The latter example is a major difference from the German procedure rules, according to which the claimant has to initiate each and every procedural act. An Estonian bailiff has the right, and hence the duty, to lead the proceedings to a successful end; the claimant has its means to influence the course of the proceedings, but the end of the proceedings does not directly depend on the use of these means. Therefore, it may be said that where the bailiff has discretionary power, he or she has to take a decision, while waiting or delaying infringes the claimant's rights.

Misuse of discretionary power is probably the most significant conflict with constitutional values that may arise in the course of discretion, and results in a breach of the principles of proportionality and equal treatment. Misuse may also be understood as discretion not complying with the objective of law, e.g., when a bailiff determines the order of seizure of assets not in view of the speed of meeting the claim and the interests of the debtor, but according to the method of sale requiring the least procedural acts. As a bailiff can, in principle, excessively impinge on the parties' fundamental rights, i.e. violate those rights, a bailiff can be considered the addressee of fundamental rights because of his authority to use the state's power of duress.^{*46}

When reviewing an appeal against a bailiff's decision or act, a court can establish a discretionary error and order the bailiff to review the matter again, or the court can take its own decision, for example, and cancel the decision to suspend the proceedings. However, a court can only review lawfulness, but not expedience, because by using undefined legal concepts, etc., the legislature has admitted to the competence of an applier of law.^{*47} The latter position is arguable in German legal literature^{*48}, but the Supreme Court has referred to this approach, stating that when an appeal is filed against a bailiff's acts, the lawfulness of the bailiff's activity will be checked, but the court is not competent to determine the price of the debtor's movables instead of the bailiff where a claim is made on these assets. Based on the duties of the bailiff as established by the CEP and the rights given to perform these duties, as well as the rights given to the debtor, a bailiff has a central role in the enforcement of claims and the objective of ensuring the protection of the claimant's interests by way of compulsory execution of the claim after the debtor has failed to perform his or her obligation voluntarily.^{*49}

4. Conclusions

As regards the legal status of the body conducting proceedings, the Estonian bailiff is the most similar to his or her French, Belgian, and Slovak counterparts. At the same time, the Estonian enforcement procedure is a universal procedure for the execution of enforcement instruments issued as a result of a large number of state proceedings.

From the viewpoint of enforcing a claim which has been recognised by the state, the nature of the claim — whether it is a private or public law claim — makes no difference. Therefore, in the European Union context, it would be reasonable to mutually recognise other enforcement instruments in addition to those arising from civil relationships, by addressing the so-called mobile debtors. Current European discussions are motivated purely by the protection of enterprise and private persons' interests and do not concern public interests.

⁴⁵ H. Maurer. *Allgemeines Verwaltungsrecht*. München: Verlag C. H. Beck 2004, pp. 140–141.

⁴⁶ B. Weber-Dürler. *Grundrechtseingriffe*. – U. Zimmerli (ed.). *Die neue Bundesverfassung. Konsequenzen für Praxis und Wissenschaft*. Berner Tage für die juristische Praxis 1999. Bern: Stämpfli Verlag 2000, p. 136.

⁴⁷ H. Maurer (Note 45), p. 144 ff.

⁴⁸ *Ibid.*, p. 147.

⁴⁹ CCSCr 28 March 2000, 3-2-1-41-00, item 4. Available at <http://www.nc.ee/?id=11&indeks=0,2,237,1708&tekst=RK/3-2-1-41-00> (8.05.2008) (in Estonian).

When establishing minimum requirements for the organisation of compulsory execution in the Member States, uniform procedure rules should also be recommended for the compulsory execution of all claims. Enforcement of different claims by different bodies is a matter of habit and tradition rather than the efficiency of proceedings. A single body conducting the proceedings can avoid the race between duress procedures where several claims are being enforced against one person.

The aspect of being a freelancer together with a bailiff's great independence and a relatively broad decision-making competence renders the Estonian enforcement proceedings efficient, which is why the search for an efficient procedural system in Europe should certainly consider the option of a freelance bailiff, which allows for a saving for the state, while ensuring efficient compulsory execution for the claimant via the fact that the bailiff's fee depends directly on the work done. The efficiency of proceedings is supported by leaving as many individual procedural issues as possible up to the bailiff to decide, without forgetting the errors that may arise from and potential misuse of discretion. Protection of the debtor's fundamental rights should, in any case, be ensured in a uniform manner regardless of the results of classification of duress procedures. The claimant's benefit protected by the proceedings differs by type of claim; in the event of a private claim, the protected benefit is the right of ownership; where the claimant is a public entity, it has no fundamental rights and the impingement of the debtor's interests is based on public interest or something similar. In the conflict of interests arising from compulsory execution, it is often the bailiff who has to find the balance between the parties, based always on the particular circumstances of the case. The choice of legal remedies available to the parties to the proceedings is thus important and one should not forget that a function of the authority of the state is being exercised regardless of whether the enforced claim is a private or public claim. The latter has relevance to the scope of competence given to the body conducting the proceedings, supervision, and possible free competition.



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Beteiligungsmodelle im neuen Estnischen Strafgesetzbuch

Begrenzung zwischen Täterschaft und Teilnahme durch Tatherrschaftslehre

Im Jahre 2002 ist in Estland im Gebiet des Strafrechts ein neues Ära begonnen; statt alten StGB (*Kriminaalkoodeks*) ist das neue StGB (*Karistusseadustik*) am 1. September 2002 in Kraft getreten.^{*1} Das war eine prinzipielle Erneuerung sowohl für die Theorie als auch für die Praxis, eine ganz neue rechtsdogmatische Lage; endete ein Prozess, der sogar als Kampf um das neue Strafrecht genannt wurde und der vom Wunsch „im estnischen Strafrecht endlich auf Leitlinien des Zentralkomitees der kommunistischen Partei der Sowjetunion zu verzichten“ getragen wurde.^{*2} Das alles hat auch natürlich die Beteiligungslehre des Strafrechts getroffen, die berechtigt als ein zentrales Gebiet des Strafrechts genannt wird, dass sowohl wegen des Umfangs als auch wegen der Kompliziertheit der Probleme.^{*3} Im Folgenden wird versucht die Beteiligungsprinzipien des neuen StGB zu schildern und kurz zu untersuchen, zu welchen Folgerungen estnische Strafrechtsdogmatik -und Praxis dabei gekommen ist.

1. Übergang zum neuen System – die Prinzipien der bisherigen Beteiligungslehre

Paragraph 17 I StGB der Estnischen Sozialistischen Sowjetrepublik von 1961 definierte die Teilnahme als vor-sätzliche gemeinsame Beteiligung von zwei oder mehr Personen an der Begehung eines Verbrechens. Wie im russischen Original war auch in der estnischen Übersetzung eine gewisse Tautologie feststellbar: Teilnahme (estn. *osavõtt*, russ. *součastie*) wurde nämlich als Beteiligung (estn. *osavõtmine*, russ. *učastie*) definiert. Als Teilnehmer kamen – außer dem Täter – der Organisator^{*4}, der Anstifter und der Gehilfe infrage (§ 17 II StGB).^{*5} In der sow-

¹ RT I 2001, 61, 364 (auf Estnisch).

² J. Sootak. Kuriteomõiste ja kuriteokoosseis. Eesti kehtiva kriminaalõiguse tegelikest allikatest (Der Begriff der Straftat und Tatbestand. Über die tatsächlichen Quellen des in Estland geltenden Strafrechts). – Juridica 1997/5, S. 225 (auf Estnisch).

³ J. Sootak. Kaks aastat karistusseadustikku – uus õigus ja uued probleemid? (Zwei Jahre neues Strafgesetzbuch: neues Recht und neue Probleme?) – Juridica 2005/1, S. 35 (auf Estnisch).

⁴ 4 § 17 IV StGB a.F. lautete: „Organisator ist eine Person, die die Begehung eines Verbrechens organisiert oder dessen Begehung geleitet hat.“

⁵ Teilnahme war ein Oberbegriff, der seinerseits Täterschaft und Teilnahme im engeren Sinn umfasste. Die Rechtsfigur des Organisators eines Verbrechens wurde beibehalten, aber als ein Typus des Teilnehmers im engeren Sinne auch im Gesetzestext genannt (§ 17 V StGB). In den Kommentaren wurden zwei verschiedene Arten der Klassifizierung der Teilnahme unterschieden: erstens die *Formen* der Teilnahme, darunter

jetischen Strafrechtslehre hat man dennoch die Notwendigkeit hervorgehoben, die Formen der Teilnahme und die Typen der Teilnehmer zu unterscheiden. Während die Formen der Teilnahme auf die typischen Merkmale einer gemeinsamen kriminellen Tätigkeit abstellten, bezogen sich die Typen der Teilnehmer vorrangig auf die individuelle Tätigkeit jedes einzelnen Teilnehmers. Man versuchte dabei die zwei Kriterien der Klassifizierung derart zu vereinigen, dass die Teilnahme als gemeinsame verbrecherische Tätigkeit mit einem gemeinsamen verbrecherischen Zweck verstanden wurde, die sich in drei Formen äußern konnte: als einfache (russ. *prostoe*) Teilnahme (d.h. als Mittäterschaft), als zusammengesetzte (russ. *složnoe*) Teilnahme (oder Teilnahme im engeren Sinne, d.h. als Teilnahme mit „Rollenverteilung“) und als verbrecherische Organisation.^{*6}

Dieses System der strafrechtlichen Teilnahme ist auch in die estnische Strafrechtsdogmatik der sowjetischen Ära übernommen worden, die sich des oben beschriebenen Sprach- und Begriffsgebrauchs bedient hat.^{*7}

Die dargelegten theoretischen Grundlagen waren prägend für die Anwendung der Rechtsfigur der Teilnahme sowohl während der Gültigkeit der damaligen sowjetischen Strafgesetzbücher als auch nach der Einführung einer neuen Fassung des am 1. Juli 1992 in Kraft getretenen estnischen StGB.^{*8} Das bedeutet, dass bis zum Inkrafttreten des neuen StGB im Jahr 2002 die Teilnahme als verbrecherische Tätigkeit mehrerer mit einem gemeinsamen verbrecherischen Zweck verstanden wurde. Diese Voraussetzungen mussten sowohl bei der Mittäterschaft als auch bei der Anstiftung und der Beihilfe erfüllt sein.^{*9} Dabei hat aber das Staatsgericht^{*10} in ständiger Rechtsprechung betont, dass die konkrete Beteiligungsform (Mittäterschaft, Anstiftung, Beihilfe sowie das Organisieren einer Straftat) stets genau zu bezeichnen ist.^{*11}

Wie das estnische Strafrecht aus der Zeit der staatlichen Selbstständigkeit vor dem Zweiten Weltkrieg hatten auch das zaristische und das sowjetrussische Strafrecht (ebenso das der Estnischen SSR) ihren Ursprung in der klassischen und neoklassischen Strafrechtsschule. Das bedeutete erstens, dass das Modell der Strafbarkeit von Einzelpersonen auf dem sogenannten restriktiven Täterbegriff beruhte, und zweitens, dass als Teilnahme-theorie die formal-objektive Theorie Anwendung fand, ohne dass jedoch auf die entsprechende Bezeichnung der Theorie hingewiesen wurde. In der Rechtsprechung des estnischen Staatsgerichts finden sich zahlreiche Urteile, welche täterschaftliche Begehung ausschließlich bei eigenhändiger Erfüllung des Tatbestands annehmen und andere an der Straftat beteiligte Personen als Teilnehmer im engeren Sinne (Organisator, Anstifter oder Gehilfe) eingestuft haben.^{*12}

Die novellierte Fassung des estnischen StGB von 1992 galt bis 2002 und wurde erst dann durch das neue StGB Estlands ersetzt. Das heute in Estland geltende StGB wurde am 6. Juni 2001 verabschiedet und ist am 1. September 2002 in Kraft getreten.^{*13} Die mit diesem Gesetzeswerk vollzogene Reform bedeutete sowohl für die Rechtsfigur der Tatbeteiligung wie auch für das gesamte estnische Strafrechtssystem eine vollständige Abkehr von den sie *bis dato* prägenden Einflüssen der russischen und sowjetischen Strafrechtsdogmatik. Als Vorbild für das gesamte neue estnische Rechtssystem und insbesondere für das neue Strafrecht wurden das deutsche Rechtsmodell und die ihm zugrunde liegende Dogmatik verwendet.^{*14}

Das heute in Estland geltende Strafrecht hat den restriktiven Täterbegriff beibehalten, da die neuere Strafrechtsentwicklung in Europa und insbesondere die deutschen Erfahrungen gezeigt haben, dass der extensive Täterbegriff sich durch keine praktischen Vorteile auszeichnet und sich auch im Hinblick auf die Rechts-

ihre besonders gefährliche Form, nämlich die organisierte Gruppe, und zweitens die *Typen* der Teilnehmer (Täter, Organisator, Anstifter, Gehilfe). Vgl. z.B. K. Paas (Hrsg.). Eesti NSV kriminaalkodeksi. Kommenteeritud väljaanne (Strafgesetzbuch der Estnischen SSR. Kommentierte Ausgabe). Tallinn 1962, § 17 Komm. 4 f (auf Estnisch).

⁶ Vgl. N. A. Beljajev (Hrsg.). Kurs sovetskogo ugolovnogo prava. Tschast obschtschaja. Tom 1 (Kursus des sowjetischen Strafrechts. Allgemeiner Teil, Bd. 1). Leningrad 1968, S. 603 f. In dem heute in Russland geltenden Strafrecht ist von diesem System vieles beibehalten worden, wie die §§ 33 und 35 des russischen StGB von 1996 belegen.

⁷ Vgl. I. Rebane (Hrsg.). Eesti NSV kriminaalkodeksi. Kommenteeritud väljaanne (Strafgesetzbuch der Estnischen SSR. Kommentierte Ausgabe). Tallinn 1980, § 17 Komm. 4a, 5, 12 (auf Estnisch).

⁸ Vgl. das Gesetz über die Einführung der neuen Fassung des StGB der Estnischen SSR. – RT I 1992, 20, 287 (auf Estnisch). Näheres zur Strafrechtsreform in Estland und über das neue StGB vgl. J. Sootak, P. Pikamäe. Einheit der verfassungsmäßigen Rechtsordnung: Entscheidungen und Lösungen im Strafrecht. – Juridica International 2002 (7), S. 127–137.

⁹ So z.B. in der Entscheidung des Estnischen Staatsgerichts (ESG) Nr. 3-1-1-1-99. – RT III 1999, 7, 70 (auf Estnisch).

¹⁰ Das estnische Staatsgericht besteht aus vier Kammern (estnisch *Kollegium*): aus einer Zivil-, einer Straf-, einer Verwaltungs- und einer Verfassungskammer. Bei den in diesem Aufsatz zitierten Entscheidungen handelt es sich um Urteile der Strafkammer (des *Kriminalkollegiums*).

¹¹ Vgl. z.B. ESG Nr. 3-1-1-64-99. – RT III 1999, 22, 217 (auf Estnisch); Nr. 3-1-3-9-00. – RT III 2000, 5, 49 (auf Estnisch).

¹² Vgl. z.B. ESG Nr. 3-1-1-1-99. – RT III 1999, 7, 70 (auf Estnisch); Nr. 3-1-1-64-99. – RT III 1999, 22, 217 (auf Estnisch).

¹³ Vgl. RT 2001, 61, 364 (auf Estnisch).

¹⁴ Vgl. J. Sootak, P. Pikamäe (Hinweis 8), S. 127–137. Da eine ausgefeilte estnische Dogmatik bisher nur in Grundzügen existiert, kann innerhalb dieses Aufsatzes häufig auf das in Estland stark rezipierte deutsche Schrifttum verwiesen werden. Vgl. zu der Thematik insgesamt auch M. Luts, J. Sootak. Das estnische Strafgesetzbuch von 2002. – ZStW 2005 (117), S. 651 ff.

sicherheit nicht unbedingt positiv ausgewirkt hat.^{*15} Auf der rechtsdogmatischen Ebene findet in Estland ein Übergang zur Tatherrschaftslehre statt.

In der Reformdiskussion hat man zwar auch die Probleme der subjektiven Teilnahmetheorie erörtert, die in der deutschen Rechtsprechung vorzuherrschen schien. Die Übernahme dieser Theorie durch die Mehrheit der estnischen Strafrechtslehre stand dennoch nicht ernstlich zur Debatte. Eine Erklärung dafür liefern zum einen rechtsstaatliche Bedenken im Blick auf das Gebot der Rechtssicherheit und Bestimmtheit; dieser Gesichtspunkt ist umso bedeutender, als man es in Estland mit einer Übergangsgesellschaft zu tun hat, in der die Festlegung der rechtsstaatlichen Grundlagen des Strafrechts immer mehr an Bedeutung gewinnt. Zum anderen zeigten die Rechtsprechung sowie die rechtsdogmatische Diskussion in Deutschland, dass die subjektive Teilnahmetheorie immer mehr an Boden zugunsten der materiell-objektiven (Tatherrschafts-)Theorie verlor.^{*16}

2. Grundstruktur und Funktionen des Beteiligungsmodells im neuen Strafgesetzbuch

2.1. Einordnung der Tatbeteiligung in das Strafrechtssystem

Der Straftatbeteiligung liegen auf der rechtsdogmatischen Ebene der restriktive Täterbegriff und das dualistische Beteiligungssystem (die Ausdehnung der Strafbarkeit außerhalb des Tatbestands) zugrunde.^{*17} Paragraph des 20 StGB besagt, dass der Täter und die Teilnehmer die Tatausführenden sind.

Im Unterschied zum früheren, aus der Sowjetzeit stammenden Strafrecht gibt es im BT des geltenden StGB keine besonderen Formen der Beteiligung mehr.^{*18} Dort findet man aber viele Tatbestände, bei denen die Straftatbegehung in einer Tätergruppe oder in einer kriminellen Vereinigung^{*19} als qualifizierende Merkmale, also als erschwerende Umstände betrachtet werden. Dabei ist die kriminelle Vereinigung im BT des StGB als *delictum sui generis* kriminalisiert (§§ 255, 256 StGB).

2.2. Überblick über etwaige Kategorien der Tatbeteiligung

Mit der Reform des Strafrechts wurden in der estnischen Lehre sowohl die Begriffssystematik als auch der Sprachgebrauch präzisiert. So unterscheidet man zunächst den Begriff des (Straftat-)Ausführenden, der als Täter oder als Teilnehmer auftreten kann (§ 20 StGB). Unter Täter versteht man den Alleintäter (§ 21 I Alt. 1 StGB), den mittelbaren Täter (§ 21 I Alt. 2 StGB) und den Mittäter (§ 21 II StGB). Die Teilnehmer sind der Anstifter und der Gehilfe (§ 22 StGB). Das neue Strafrecht hat auf die Figur des Organisators verzichtet (in der Praxis wird ehemaliger Organisator häufig als Mittäter behandelt).

Der AT des StGB enthält in § 23 eine Regelung, die sowohl auf die im StGB enthaltenen Verbrechen als auch auf die in anderen Gesetzen enthaltenen Ordnungswidrigkeiten^{*20} Anwendung findet. Diese Regelung besagt, dass bei den Ordnungswidrigkeiten nur die Täterschaft, nicht aber die Teilnahme strafbar ist.

2.3. Funktionen und Auswirkungen etwaiger Kategorien der Tatbeteiligung

Der Täter wird entsprechend dem Tatbestand des BT des StGB als Alleintäter, Mittäter oder mittelbarer Täter zur Verantwortung gezogen. Für den Teilnehmer gilt, dass er nach demselben Tatbestand wie der Täter strafbar

¹⁵ Argumente gegen den sog. *Einheitstäter* siehe bei M. Ernits, P. Pikamäe, E. Samson, J. Sootak. Karistusseadustiku üldosa eelnõu. Lähetealused ja põhjendus (Entwurf des Allgemeinen Teils des StGB. Ausgangspunkte und Begründung). Tallinn 1999, § 19 Komm. 3 (auf Estnisch).

¹⁶ So z.B. W. Joecks. Strafgesetzbuch. Studienkommentar. 3. Aufl. München 2001, § 25 Rn. 3; J. Wessels, W. Beulke. Strafrecht. Allgemeiner Teil. 32. Aufl. Heidelberg 2002, Rn. 516; R. Schmidt. Strafrecht. Allgemeiner Teil. 3. Aufl. Grasberg 2004, S. 351.

¹⁷ Vgl. dazu z.B.: H.-H. Jescheck, Th. Weigend. Lehrbuch des Strafrechts. Allgemeiner Teil. 5. Aufl. Berlin 1996, § 61 III 1, S. 648; J. Wessels, W. Beulke (Hinweis 16), Fn. 505; B. Heinrich. Strafrecht. Allgemeiner Teil II. Stuttgart 2005, Fn. 1174.

¹⁸ Wie z.B. § 58¹¹ StGB der UdSSR von 1926 oder § 70 StGB der Estnischen SSR von 1961.

¹⁹ Es handelt sich hier um Mittäterschaft im Sinne von § 21 II StGB, so z.B. § 199 II 7 StGB (Gruppeneinbruch).

²⁰ Diese ca. 200 Ordnungswidrigkeitstatbestände sind nur zum kleineren Teil im BT des StGB zu finden, mehrheitlich sind sie in Nebengesetzen, also in Gesetzen, die einen konkreten, abgeschlossenen Lebensbereich regeln (wie z.B. das Straßenverkehrsgesetz) und neben den allgemeinen Regelungsnormen auch Strafnormen enthalten.

ist, wenn die gesetzliche Regelung bezüglich eines besonderen persönlichen Merkmals (§ 24 StGB) keine anders lautende Subsumtion vorschreibt (§ 22 IV StGB).

3. Darstellung der einzelnen Beteiligungsformen

3.1. Täterschaft

3.1.1. Alleintäterschaft

Alleintäter ist die Person, welche die Straftat als unmittelbarer Täter selbst begeht (§ 21 I Alt. 1 StGB). Während das alte StGB den Täter als die Person definierte, welche die Tat unmittelbar begeht, bestimmt das geltende StGB, dass der Alleintäter die Straftat selbst begeht.^{*21} Die Figur der Nebentäterschaft – wenn auch dem geltenden StGB und der Rechtsprechung nicht bekannt – wird in der Literatur behandelt.^{*22}

Der Täter wird – entsprechend der Formulierung des konkreten Tatbestands des BT des StGB – als Alleintäter, mittelbarer Täter oder Mittäter zur Verantwortung gezogen. Nach den Richtlinien des Justizministeriums^{*23} wird die vom Täter begangene Straftat im Urteilstenor^{*24} grundsätzlich nur als Tatbestand des BT ausgewiesen; die Straftatsubsumtion benötigt also hinsichtlich der Täterschaft keinen Verweis auf § 21 StGB.^{*25}

Der Alleintäter, der die besonderen vom Gesetz verlangten persönlichen Merkmale (Qualifikationen) nicht besitzt, wird nach dem Grundtatbestand zu bestrafen sein, während das Vorhandensein der entsprechenden Merkmale beim Alleintäter zur Anwendung des qualifizierten Tatbestands führt.^{*26} Im estnischen Strafrecht ist grundsätzlich nur die vorsätzliche Begehungsform strafbar; die Fahrlässigkeit muss nach § 15 I StGB im speziellen Tatbestand ausdrücklich unter Strafe gestellt sein.

3.1.2. Mittäterschaft

Bis zur Strafrechtsreform 2001 ging die estnische Rechtsprechung grundsätzlich von den Voraussetzungen der formal-objektiven Teilnahmetheorie aus.^{*27} Es lässt sich feststellen, dass die Gerichte zumindest in all den Fällen den Begriff der Mittäterschaft sehr weit aufgefasst haben, in denen alle Mittäter am Tatort anwesend waren, was dazu geführt hat, dass der Übergang zur Tatherrschaftstheorie grundsätzlich erleichtert wurde.^{*28} Dabei machte das Staatsgericht allerdings eine wesentliche Einschränkung: Die Allein- und Mittäterschaft sowie die Beihilfe seien durch das Merkmal unmittelbar (§ 17 III StGB a.F.) zu unterscheiden, d.h. für die Mittäterschaft seien ausschließlich eigene tatbestandsmäßige Handlungen erheblich. Demnach konnte als

²¹ Vgl. J. Sootak, P. Pikamäe (Hrsg.). Karistusseadustik. Kommenteeritud väljaanne (Strafgesetzbuch. Kommentierte Ausgabe). 2. Aufl. Tallinn 2004, § 21 Komm. 3 (auf Estnisch).

²² Vgl. z.B. J. Sootak. Täideviimine ja osavõtt (Täterschaft und Teilnahme). Tallinn 2004, S. 47 (auf Estnisch). Auch in Kommentaren zum StGB wird der Begriff „Nebentäter“ nicht verwendet, die entsprechende Rechtsfigur wird aber als *objektive Beteiligung von mehreren Personen* beschrieben. Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 21 Komm. 7.

²³ Vgl. die Verordnung des Justizministers vom 23.8.2002 Nr. 54. – RTL 2002, 95, 1480 (auf Estnisch).

²⁴ Hierbei handelt es sich um den sog. *Resolutivteil*, der in Estland am Anfang des Urteils steht.

²⁵ Das bedeutet, dass z.B. der Alleintäter eines Diebstahls nur unter Nennung von § 199 I StGB verurteilt wird – im Urteilstenor erfolgt also kein Verweis auf § 21 I StGB; ebenso wenig wird bei der Mittäterschaft (z.B. bei § 199 II 7 StGB [Gruppeneinbruch]) auf § 21 II StGB verwiesen. Hingegen muss eine Verantwortlichkeit wegen Versuchs, Unterlassens oder Teilnahme im Urteilstenor ausdrücklich ausgesprochen werden.

²⁶ U.U. auch zur Bejahung der Mittäterschaft.

²⁷ So war es erforderlich, dass alle Mittäter am Tatort anwesend waren und jeder von ihnen mindestens ein Merkmal des objektiven Tatbestands verwirklicht hat; bei Sonderdelikten mussten auch alle Mittäter den Anforderungen der Täterqualität entsprechen. Vgl. z.B. ESG Nr. 3-1-1-49-97. – RT III 1997, 17, 177 (auf Estnisch). So hat ein Gericht z.B. in einem Fall Mittäterschaft bei einem Diebstahl bejaht, in dem mehrere Diebe gemeinsam eine fremde Wohnung betreten und gemeinsam ein TV-Gerät weggetragen hatten. Siehe ESG Nr. 3-1-3-20-98. – RT III 1998, 30, 297 (auf Estnisch); 3-1-1-1-99. – RT III 1999, 7, 70 (auf Estnisch). Man findet aber auch Gerichtsentscheidungen, bei denen die Eigenhändigkeit des einzelnen Tatbeitrags im obigen Sinne nicht als unbedingt erforderlich angesehen wurde, obwohl sich zwar alle Mittäter am Tatort befanden, die Kausalität zwischen den Handlungen (z.B. einem Faustschlag) einzelner Mittäter und dem Erfolg (z.B. dem Tod des Opfers) aber nicht unbedingt festgestellt werden musste, vgl. z.B. ESG Nr. 3-1-1-29-01. – RT III 2001, 19, 198 (auf Estnisch). Nach Meinung des Staatsgerichts beruhte die Mittäterschaft in solchen Fällen auf dem gemeinsamen, von allen Mittätern verfolgten Zweck der strafbaren Handlung, vgl. z.B. zur Mittäterschaft bei Totschlag ESG Nr. 3-1-1-101-96 (RT III 1996, 31, 397; auf Estnisch), bei Raub ESG Nr. 3-1-1-126-96 (RT III 1997, 3, 19; auf Estnisch), Nr. 3-1-1-116-98 (RT III 1999, 2, 21; auf Estnisch). Näheres zu den Entscheidungen des Staatsgerichts hinsichtlich der Anwendung der formal-objektiven Theorie bei P. Pikamäe. Kaastäideviimise määratlemine Karistusseadustik ja Riigikohtu praktika (Feststellung der Mittäterschaft. Strafgesetzbuch und Praxis des Staatsgerichts). – Juridica 2003/3, S. 148 f (auf Estnisch).

²⁸ Ein erstes Urteil mit einer solchen Tendenz wurde schon am 7.10.1997 erlassen. Das Gericht weist darin direkt auf die materiell-objektive Theorie hin als einen „die Mittäterschaft erweiternden Begriff“. Bei der Mittäterschaft – so das Gericht – geht man von der funktionellen Tatherrschaft aus, d.h. die Mittäter handeln in einer Weise gemeinsam, dass jeder die Tat beherrscht, und setzt voraus, dass die Erfüllung des Tatbestands von jedem einzelnen Mittäter abhängt. Beherrscht einer der Handelnden die Tat nicht, ist er kein Täter.

Mittäter nur eine Person angesehen werden, die den Tatbestand unmittelbar erfüllte.^{*29} Diese und in der Nachfolgezeit erlassene ähnlich lautende höchstrichterliche Entscheidungen^{*30} ernteten scharfe Kritik in der Strafrechtslehre.^{*31} Der Standpunkt des Staatsgerichts lässt sich vor allem damit erklären, dass das in § 17 III StGB a.F. vorgesehene Merkmal unmittelbar eine weitergehende Formulierung kaum ermöglicht hätte. Nicht zu übersehen ist dabei allerdings, dass gerade diese Urteile des Staatsgerichts den Weg zur Anwendung der Tatherrschaftstheorie eröffnet haben. Es ist nämlich der Ansicht zuzustimmen, dass die Tatherrschaftstheorie eine Fortentwicklung der formal-objektiven Theorie ist und die Täterschaft auch in solchen Fällen für möglich hält, in denen der Betreffende die Ausführungshandlung nicht selbst vornimmt. Die auf der materiell-objektiven Theorie aufbauende Tatherrschaftslehre hat die Lücken der formal-objektiven Theorie auf diese Art und Weise vermieden.^{*32}

Da der Täterbegriff nach geltendem StGB nur durch das Merkmal selbst bestimmt wird, ist die persönliche Erfüllung der Tatbestandsmerkmale durch einen Täter (Mittäter) nach allgemeinem Verständnis der estnischen Rechtsprechung und Lehre nicht mehr erforderlich. Damit scheint ein weiterer Schritt der Ausweitung der Tatherrschaftstheorie auf die estnische Beteiligungslehre vollzogen zu sein.^{*33}

Auch wenn die Tatherrschaftslehre durch die Rechtsprechung des Staatsgerichts bestätigt wurde, gilt sie in Estland noch nicht in vollem Umfang.^{*34}

Zum Zweck der Vereinheitlichung der Rechtsprechung bezüglich der Mittäterschaft hat das Staatsgericht in einem Urteil^{*35} folgende Feststellungen als *obiter dicta* getroffen:

- Alle Mittäter müssen gemäß § 21 II 2 StGB gemeinsam und übereinstimmend handeln. Die Straftat ist dann gemeinsam begangen, wenn die Mittäter das Geschehen im Sinne eines arbeitsteiligen und funktionalen Zusammenwirkens beherrschen. Das bedeutet, dass jeder Mittäter einen wesentlichen Tatbeitrag zu der einheitlichen Tat leisten muss, von dem die Verwirklichung des gemeinsamen Ziels abhängt.^{*36} Es ist nicht erforderlich, dass die einzelnen Mittäter selbst vollständig oder teilweise den objektiven Tatbestand verwirklichen. Die einzelnen Mittäter müssen also bei der Planung und der Ausführung der Tat nicht in gleicher Weise tätig werden. Das bedeutet, dass innerhalb der Mittätergruppe eine Person der anderen untergeordnet sein kann, was aber ihre strafrechtliche Stellung als Mittäter nicht berührt.
- Die subjektive Seite der Mittäterschaft zeichnet sich durch einen gemeinsamen Tatentschluss aus, was bedeutet, dass eine Vereinbarung über die Straftatbegehung im Sinne von § 21 II 1 StGB getroffen worden sein muss. Die Mittäter müssen verabredet haben, die Straftat gemeinsam zu begehen; dabei werden ihre einzelnen Rollen und – unter Umständen auch – ihre gegenseitige Abhängigkeit festgelegt. Jeder Mittäter betrachtet seinen Tatbeitrag als einen notwendigen Bestandteil der gemeinsamen kriminellen Tätigkeit. Die Vereinbarung muss nicht notwendigerweise mündlich und vor dem unmittelbaren Ansetzen zur Tatbegehung (also im Vorbereitungsstadium) geschlossen worden sein; sie kann auch stillschweigend oder konkludent während der Begehung der Straftat erfolgen.^{*37}

²⁹ In dem einschlägigen Fall ging es um Geldfälschung, so dass als Täter nur diejenige Person fungieren konnte, die unmittelbar die gefälschten Geldscheine gedruckt hatte. Der Angeklagte hatte aber nur das Kopiergerät und die Farbkassetten besorgt sowie das Gerät technisch betriebsbereit gehalten, weswegen er nicht als Täter, sondern nur als Gehilfe qualifiziert werden konnte, vgl. ESG Nr. 3-1-1-98-97. – RT III 1998, 1, 1 (auf Estnisch).

³⁰ Siehe z.B. ESG Nr. 3-1-1-23-01. – RT III 2001, 8, 91 (auf Estnisch).

³¹ Man warf diesen Gerichtsentscheidungen vor, dass sie sich einerseits auf die Tatherrschaftstheorie beriefen, sich aber andererseits innerhalb der formal-objektiven Theorie bewegten und zwar durch die Verwendung des Merkmals *unmittelbar*. Vgl. dazu ausführlich P. Pikamäe (Hinweis 27), S. 149.

³² Vgl. z.B. W. Joecks (Hinweis 16), § 25 Rn. 5; ebenso R. Schmidt (Hinweis 16), S. 350.

³³ Im Urteil vom 14.3.2003 hat das Staatsgericht eine wegweisende Entscheidung im Sinne der weiten Tatherrschaftstheorie getroffen. Es stellt zunächst fest, dass das neue StGB zwar auf die Rechtsfigur des *Organisators* verzichtet hat, dass aber „die Person, die sich an der Vorbereitung eines Verbrechens mit einem wesentlichen Tatbeitrag beteiligt hat, und der Organisator eines Verbrechens in der Regel als *Täter* [d.h. hier als Mittäter] zu betrachten sind“. Da aber die einschlägige Straftat in der Geltungszeit des alten StGB begangen worden und nach § 3 II des Einführungsgesetzes zum neuen StGB (RT I 2002, 56, 350; auf Estnisch) deshalb das alte StGB anzuwenden war, wurde die Frage der Mittäterschaft nach dem alten StGB und seiner formal-objektiven Theorie gelöst (vgl. dazu das Urteil des Staatsgerichts Nr. 3-1-1-20-03). Ein weiterer Fall gab dem Staatsgericht noch einmal die Möglichkeit, seinen Standpunkt im Sinne der Tatherrschaftstheorie darzulegen. Das Gericht führte in seinem Urteil vom 20.6.2003 – sich dabei auf das Urteil ESG Nr. 3-1-1-23-01 berufend – aus, dass nach der Tatherrschaftstheorie als Täter die Person anzusehen ist, welche die Tat beherrscht und diese nach ihrem Willen leiten, aber auch aufhalten kann. Die Mittäterschaft besteht in der Erfüllung der objektiven und subjektiven Merkmale, die zeigen, wessen Handlungen den gewichtigen Teil bei der Verwirklichung des Tatbestands gebildet haben und wessen Wille die Tat gesteuert hat, vgl. ESG Nr. 3-1-1-88-03. – RT III 2003, 25, 253 (auf Estnisch).

³⁴ Der Grund ist darin zu sehen, dass auch in dem vom Staatsgericht entschiedenen Fall die beiden Mittäter der Erpressung am Tatort anwesend waren und schon aus diesem Grund das Tatbestandsmerkmal der „Unmittelbarkeit“ erfüllt hatten.

³⁵ Siehe ESG Nr. 3-1-1-97-04. – RT III 2005, 4, 36 (auf Estnisch).

³⁶ Siehe ESG Nr. 3-1-1-97-04, Z. 21.1.

³⁷ Siehe ESG Nr. 3-1-1-97-04, Z. 21.2.

- Im Unterschied zur formal-objektiven Theorie ist eine vereinbarte und gemeinsam begangene Straftat als eine Ganzheit anzusehen; sie ist unteilbar und als solche allen Mittätern auch dann zurechenbar, wenn einzelne Mittäter nur einzelne Tatbeiträge eigenhändig geleistet haben. Diese gemeinsame Tat umfasst alle unwesentlichen Abweichungen der tatbestandsmäßigen Tätigkeit der Mittäter, die nicht als Exzess zu betrachten sind. Damit wird die Meinung begründet, dass § 21 II 2 StGB – der Tatherrschaftstheorie folgend – eine Zurechnungsnorm darstellt, nach der jedem Mittäter die Handlungen anderer Mittäter zugerechnet werden. Alle Mittäter müssen allerdings nicht nur allgemein Täterqualität besitzen (z.B. die geistige Zurechnungsfähigkeit), sondern auch die besonderen persönlichen Merkmale (wie z.B. bei Amtsdelikten das Merkmal des Amtsträgers).^{*38}
- Jeder Mittäter muss das strafbare Geschehen kontrollieren können. Ist ein Tatbeitrag bereits in der Phase der Vorbereitung einer Straftat geleistet worden, stellt dies allein kein Hindernis dar, eine Mittäterschaft zu bejahen.^{*39}

Aus diesen Vorgaben des Staatsgerichts lässt sich die Meinung ableiten, dass die Tatherrschaftstheorie ein fester Bestandteil der estnischen Rechtsprechung bezüglich der Teilnahmelehre geworden ist. Dabei ist zu merken, dass Staatsgericht sog. extensive Tatherrschaftslehre angenommen hat und schon die Mitwirkung im Vorbereitungsstadium für die Mittäterschaft ausreichen lässt.^{*40} Im Schrifttum wurde es als „radikale Stellungnahme“ bezeichnet.^{*41}

Infolge der Bejahung einer Mittäterschaft (§ 21 II 2 StGB) kommt entweder die Strafbarkeit der Mittäter wegen des Grunddelikts infrage (z.B. wegen Totschlags, § 113 StGB) oder – wenn sich die Qualifikation auf ein entsprechendes besonderes persönliches Merkmal bezieht – wegen eines Verbrechens, das in einer Gruppe begangen worden ist (z.B. wegen Gruppeneinbruches, § 199 II 7 StGB).^{*42}

Im BT des estnischen StGB finden sich viele Tatbestände, in denen als qualifizierendes Merkmal – d.h. als erschwerender Umstand – die Straftatbegehung in einer Gruppe (Mittäterschaft im Sinne von § 21 II StGB) oder in einer kriminellen Vereinigung auftritt. Das Staatsgericht hat in vielen seinen Urteilen besonders hervorgehoben, dass das Merkmal „Begehung einer Straftat in einer Gruppe“ als Mittäterschaft gemäß § 21 II StGB und im Sinne der Tatherrschaftslehre aufzufassen ist.^{*43}

Es sind keine Urteile des Staatsgerichts bekannt, die eine Mittäterschaft bei Fahrlässigkeitsdelikten bejahen. In der Literatur wird aber eine solche Möglichkeit nicht ausgeschlossen.^{*44}

3.1.3. Mittelbare Täterschaft

Gemäß § 21 I Alt. 2 StGB kann der Täter die Straftat auch mittelbar begehen. Das Gesetz kennt allerdings die Figur der mittelbaren Täterschaft nicht; es spricht stattdessen von einem Täter, der die Straftat begeht, indem er „eine andere Person benutzt“. In Rechtsprechung und Lehre wird jedoch der Begriff „mittelbare Täterschaft“ sowohl vor als auch nach dem Inkrafttreten des neuen StGB gebraucht.^{*45}

Während in § 17 I StGB a.F. die Teilnahme als gemeinsame Beteiligung am Verbrechen definiert war, ist nun in § 22 StGB n.F. von einer rechtswidrigen Tat die Rede. Infolgedessen reicht es nach dem geltenden Strafrecht für die Abgrenzung der mittelbaren Täterschaft von der Anstiftung nicht mehr aus, dass bei der mittelbaren Täterschaft der Vordermann nicht schuldhaft handelt, d.h. z.B. als Kind unter 14 Jahren oder als Geisteskranker keine Täterqualität besitzt. Bei der Feststellung der mittelbaren Täterschaft ist die Tatherrschaft zum entscheidenden Kriterium geworden. Die Abgrenzung hängt davon ab, ob die Handlungsherrschaft des unmittelbar Handelnden von der Willensherrschaft des Hintermanns überlagert wird.^{*46}

Es reicht für die Strafbarkeit des Hintermanns aus, wenn der Tatausführende als „menschliches Werkzeug“ benutzt wird und eine Straftat, die dem Straftatbestand entspricht, in dieser „Eigenschaft“ begeht.

³⁸ Ebenda, Z. 21.3–21.4.

³⁹ Ebenda, Z. 21.5 mit Hinweisen ESG Nr. 3-1-1-23-01 und Nr. 3-1-1-20-03.

⁴⁰ Die Rechtsprechung hat diese Möglichkeit auch sehr weit benutzt. So hat Tartuer Bezirksgericht im Urteil Nr. 2-1-449/2003 eine Mittäterschaft im folgenden Fall bejaht: fünf Drogenabhängige haben gemeinsam das Geld gesammelt und ein Mitglied der Gruppe hat mit diesem Geld von Drogenhändler eine große Menge Drogen gekauft (für Eigennutz in der Gruppe) – dabei wurde er festgenommen. Bezirksgericht hat alle fünf als Mittäter des Drogengeschäfts behandelt.

⁴¹ J. Sootak. Kaks aastat karistusseadustikku (Zwei Jahre Strafgesetzbuch). – Juridica 2005/1, S. 37 (auf Estnisch).

⁴² Bei der letztgenannten Variante wird § 21 II StGB im Urteilstenor nicht zitiert, obwohl zur Feststellung der Mittäterschaft gerade diese Bestimmung die Rechtsgrundlage liefert. Der Tatbestand des Gruppeneinbruches ähnelt dem Bandendiebstahl des deutschen StGB.

⁴³ Siehe z.B. ESG Nr. 3-1-1-83-01. – RT 2001, 25, 268 (auf Estnisch); Nr. 3-1-1-106-01. – RT III 2001, 28, 307 (auf Estnisch); Nr. 3-1-1-88-03. – RT III 2003, 25, 253 (auf Estnisch).

⁴⁴ Vgl. J. Sootak (Hinweis 22), S. 67.

⁴⁵ So z.B. in der Entscheidung ESG Nr. 3-1-1-64-05. – RT III 2005, 26, 172 (auf Estnisch); I. Rebane (Hinweis 7), § 17 Komm. 11c; J. Sootak, P. Pikamäe (Hinweis 21), § 21 Komm. 4.1; J. Sootak (Hinweis 22), S. 31 ff.

⁴⁶ Näher z.B.: J. Wessels, W. Beulke (Hinweis 16), Rn. 538.

Tatherrschaft in diesem Sinn bedeutet, dass der Hintermann zu entscheiden hat, ob, wo und wie die Tat zu begehen. Tatherrschaft im Sinne der mittelbaren Täterschaft kann in drei Formen auftreten – die Willensherrschaft kraft Nötigung, kraft Irrtums oder kraft organisatorischer Machtapparate.^{*47} In einer späteren Entscheidung^{*48} hat das Staatsgericht das für die Tatherrschaft maßgebliche Erfordernis der „notwendigen Überlegenheit“ des Hintermanns wiederholt, d.h. sein Wissen über die Tat oder seinen Willen zur Tatbegehung durch den Vordermann hervorgehoben, und hat wiederholt bemerkt, dass mittelbare Täterschaft auch kraft „bestimmter Machtapparate“ möglich ist.

Damit ist festzustellen, das Staatsgericht sog. normativ-faktisches Tatherrschaftsverständnis (eingeschränkte Verantwortungsprinzip) angenommen hat und somit auch mittelbare Täterschaft im Form „Täter hinter dem Täter“ akzeptiert. In der Praxis wird es „stillschweigend“ im Gebiet der strafrechtlichen Verantwortung der juristischen Personen gemacht. Nämlich verlangt § 14 I StGB für die strafrechtliche Verantwortung der juristischen Personen, dass die Tat im Interesse von der juristischen Person vom Leiter der Firma begangen worden ist. Dementsprechend hat Staatsgericht in mehreren Entscheidungen gesagt, dass auch diejenige Leitperson als Täter zu behandeln ist, der wohl selbst keine tatbestandsmäßige Handlung vornimmt, wenn aber die Tat wegen seines Befehls oder mit seiner Beistimmung begangen worden ist.^{*49} Dabei wird aber auch unmittelbare Täter als Täter bestraft.^{*50}

Somit ist festzuhalten, dass das Staatsgericht die Tatherrschaftstheorie bei der Anwendung der mittelbaren Täterschaft grundsätzlich anerkannt hat; ihre breite Anwendung in der Rechtsprechung der unteren Gerichte steht aber noch bevor. Die Tatherrschaftslehre als dogmatische Grundlage der mittelbaren Täterschaft ist auch im estnischen Schrifttum allgemein anerkannt.^{*51}

Im neuen StGB sind verschiedene Formen des Versuchs geregelt. So bezieht sich § 25 III StGB auf den Versuch der mittelbaren Täterschaft. Danach liegt ein Versuch vor, wenn der Hintermann die Kontrolle über das Geschehen verliert oder wenn der Tatmittler nach den Vorstellungen des Hintermanns unmittelbar zur Ausführung der Straftat ansetzt.^{*52}

3.2. Teilnahme

Die Teilnahme an einer Straftat ist in zwei Formen möglich, nämlich als Anstiftung und als Beihilfe (§ 22 I StGB). Sie muss drei gesetzliche Anforderungen erfüllen:

- Im Unterschied zum früher geltenden Strafrecht, bei dem für die Bejahung der Teilnahme die Haupttat der rechtlichen Qualität eines Verbrechens entsprochen haben, d.h. also auch schuldhaft begangen worden sein musste, ist Teilnahme nach der heute geltenden Regelung an einer „nur“ rechtswidrigen, d.h. nicht unbedingt auch schuldhaft begangenen Tat möglich.^{*53}
- Die Teilnahme zeichnet sich durch den sogenannten Doppelvorsatz aus, d.h. der Vorsatz muss sowohl die Handlung der Anstiftung/Beihilfe als auch die der Haupttat selbst umfassen. Die beiden Formen der Teilnahme können in allen drei Vorsatzformen (§ 16 StGB) begangen werden.^{*54} Es reicht dabei aus, wenn der Teilnehmer sich die Umstände der Haupttat nur in groben Zügen vorstellt.^{*55} Der Teilnehmer ist auch dann strafbar, wenn die Haupttat vorsätzlich, der Erfolg aber fahrlässig verursacht wurde (§ 15 II StGB).
- Der Umstand, dass man nur an der Tat einer anderen Person teilnehmen kann, hat zur Folge, dass in Fällen, in denen der „Teilnehmer“ zuerst die Teilnahme tat verübt (Anstiftungs- oder Beihilfehandlung) und danach noch die Haupttat selbst begeht, nur als Täter strafbar ist. Den Grund dafür liefert die in der Rechtsprechung und Literatur herrschende Meinung, dass die schwerere Beteiligungsform (die Täterschaft) bei der Subsumtion die leichtere Form (die Teilnahme) „konsumiert“.^{*56} Diese aus dem früher geltenden Strafrecht übernommene Lehrmeinung ist allerdings heute umstritten.

⁴⁷ Siehe ESG Nr. 3-1-1-17-03. – RT III 2003, 17, 159 (auf Estnisch).

⁴⁸ Siehe ESG Nr. 3-1-1-24-06. – RT III 2006, 20, 183 (auf Estnisch).

⁴⁹ Siehe z.B. ESG 3-1-1-82-04. – RT III 2004, 24, 263 (auf Estnisch); 3-1-1-145-05. – RT III 2006, 7, 59 (auf Estnisch).

⁵⁰ Siehe ESG 3-1-1-100-03. – RT III 2003, 32, 326 (auf Estnisch).

⁵¹ Vgl. J. Sootak (Hinweis 22), S. 33 f.; J. Sootak, P. Pikamäe (Hinweis 21), § 21 Komm. 4.1–4.2.

⁵² Zu diesem Komplex gibt es bislang keine weiteren Stellungnahmen in der Literatur.

⁵³ Es sind jedoch bis heute keine einschlägigen Gerichtsentscheidungen bekannt, in denen der Teilnahme eine „nur“ rechtswidrige, unverschuldete Haupttat zugrunde lag.

⁵⁴ Die Vorsatzschuld kommt im estnischen Strafrecht in drei Formen vor: Absicht, direkter Vorsatz und bedingter Vorsatz (§ 16 StGB).

⁵⁵ Siehe z.B. ESG Nr. 3-1-1-94-00. – RT I 2000, 24, 261 (auf Estnisch).

⁵⁶ Siehe z.B. ESG Nr. 3-1-1-1-00. – RT III 2000, 4, 37 (auf Estnisch); Nr. 3-1-1-5-00. – RT III 2000, 4, 38 (auf Estnisch); J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 2.3.

Gemäß § 22 V StGB stellt zwar die Beihilfe gegenüber der Anstiftung die „leichtere“ Form der Teilnahme dar, dennoch ist auch hier für die Praxis die Frage von Bedeutung, ob die „leichtere“ Beihilfe von der „schwereren“ Anstiftung gleichfalls konsumiert werden kann oder nicht. Da die estnischen Gerichte *bis dato* beide Teilnahmeformen als gleichwertig betrachten, kann die Beihilfe nicht von der Anstiftung konsumiert werden.^{*57}

Beim Zusammentreffen verschiedener Teilnahmeformen liegt nach dem Verständnis der estnischen Rechtsprechung ein Fall von Realkonkurrenz der Teilnahmeformen vor.

Das estnische Strafrecht geht wie früher vom Grundsatz der limitierten Akzessorietät aus. Das bedeutet vor allem, dass eine tatbestandsmäßige Haupttat vorliegen muss, d.h. die Merkmale eines konkreten Tatbestands des BT entweder in Form der unmittelbaren oder der mittelbaren Täterschaft erfüllt worden sein müssen.^{*58} Das Erfordernis einer vorsätzlichen und rechtswidrigen Haupttat ergibt sich bereits aus dem Wortlaut von § 22 II und III StGB.

Die Haupttat muss mindestens das Versuchsstadium erreicht haben.^{*59} Auch wenn das Vorliegen der Haupttat verlangt wird, ist es aber nicht notwendig, dass der konkrete Täter bekannt ist.^{*60}

In der Lehre ist es unumstritten, dass für den *Exzess* eines Teilnehmers ausschließlich dieser selbst strafrechtlich verantwortlich ist. Der Teilnehmer haftet nur insoweit, als die Haupttat mit seinem Vorsatz übereinstimmt. Bei einem sogenannten quantitativen Exzess^{*61} wird der Haupttäter wegen der tatsächlich begangenen Tat bestraft, während der Teilnehmer bis zur Grenze seines eigenen Vorsatzes strafbar ist. Ebenso wird der Haupttäter eines sogenannten qualitativen Exzesses bestraft, der Teilnehmer bleibt aber in einem solchen Fall in Bezug auf die angestiftete Tat straffrei, da es sich hierbei um eine versuchte (erfolglose) Teilnahme handelt, die im estnischen Strafrecht nicht strafbar ist.^{*62}

Im Gerichtsurteil muss darauf hingewiesen werden, in welcher Beteiligungsform der Betroffene gehandelt hat (Anstiftung/Beihilfe), ein allgemeiner Hinweis auf die Beteiligung reicht nicht aus.^{*63}

3.2.1. Anstiftung

§ 22 II StGB bezeichnet die Anstiftung als vorsätzliches Bestimmen^{*64} eines anderen zur Begehung einer vorsätzlichen rechtswidrigen Tat. Die Lehre ist sich darüber einig, dass das Bestimmen das „Hervorrufen des Tatvorsatzes oder des Tatentschlusses beim künftigen Täter“ bedeutet.^{*65}

Die Anstiftungshandlung kann in einer beliebigen Form stattfinden. Es ist aber erforderlich, dass sich die Anstiftung kausal auf die Begehung der Haupttat auswirkt. In der Lehre findet die sogenannte Kommunikationstheorie Zustimmung, die einen geistigen Kontakt zwischen dem Anstifter und dem Täter verlangt und die bloße einseitige Schaffung günstiger Bedingungen für die Tatbegehung nicht ausreichen lässt.^{*66}

Auf der subjektiven Seite der Anstiftung können alle drei Formen des Vorsatzes vorliegen.^{*67} Für die Anstiftungstat wird ein Doppelvorsatz gefordert, d.h. der Vorsatz muss sowohl die Anstiftungshandlung als auch die Vollendung der Haupttat selbst umfassen.

⁵⁷ Siehe hierzu z.B. ESG Nr. 3-1-1-34-03 (RT III 2003, 14, 133, auf Estnisch) – eine Entscheidung, die jedoch nicht im Einklang mit § 22 V StGB steht. Selbstverständlich ist auch ein Fall der Realkonkurrenz der Beteiligungsformen in Bezug auf unterschiedliche Tatbestände des BT denkbar (z.B. Täterschaft der Urkundenfälschung und Beihilfe zum Gebrauch der gefälschten Urkunde), vgl. z.B. ESG Nr. 3-1-1-1-00. – RT III 2000, 4, 37 (auf Estnisch).

⁵⁸ Siehe z.B. ESG Nr. 3-1-1-34-03. – RT III 2003, 14, 133 (auf Estnisch); Nr. 3-1-1-94-00. – RT III 2000, 24, 261 (auf Estnisch). In der Entscheidung ESG Nr. 3-1-1-60-00 (RT III 2000, 15, 165; auf Estnisch) hat das Staatsgericht verlangt, dass auch – sofern die Haupttat durch aktives Tun begangen wird – die Teilnahmetat in Form aktiven Tuns begangen werden muss (wörtlich: in einem „proportionalen“ Verhältnis zur Haupttat stehen muss). Demnach genügt Unterlassen dann nicht. Allerdings muss auch festgehalten werden, dass in späteren Entscheidungen des Staatsgerichts dieser Standpunkt nicht mehr vertreten wird.

⁵⁹ Siehe z.B. ESG Nr. 3-1-1-94-00. – RT III 2000, 24, 261 (auf Estnisch).

⁶⁰ Siehe z.B. ESG Nr. 3-1-1-129-96. – RT III 1996, 3, 22 (auf Estnisch).

⁶¹ Beim quantitativen Exzess tut der Haupttäter mehr, als der Anstifter von ihm verlangt hat; beim qualitativen Exzess begeht der Tatmittler eine andere Tat als die, zu der er verleitet wurde.

⁶² J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 7; J. Sootak (Hinweis 22), S. 68. Siehe auch unten I.C.2.a.

⁶³ Siehe ESG Nr. III-1/1-79/95. – RT III 1996, 3, 38 (auf Estnisch).

⁶⁴ Wörtlich: „Biegen“ bzw. „Neigen“ (estn. *kallutamine*); inhaltlich gleicht dieser Begriff dem *Bestimmen* im Sinne von § 26 des deutschen StGB.

⁶⁵ Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 6.1.

⁶⁶ Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 5, 6.1. Einschlägige Entscheidungen sind in der Rechtsprechung des Staatsgerichts nicht zu finden.

⁶⁷ Darunter also auch der bedingte Vorsatz, siehe ESG Nr. 3-1-1-28-02. – RT III 2002, 12, 129 (auf Estnisch).

Bei der Handlung eines *agent provocateur* ist die Strafbarkeit für Anstiftung wegen des Fehlens des subjektiven Tatbestands ausgeschlossen.^{*68} Es liegt keine Anstiftung im strafrechtlichen Sinn vor, wenn der Vorsatz des Anstifters, der als *agent provocateur* tätig ist, nur bis zum Versuchsstadium reicht, d.h. es würde sich nur um eine Anstiftung zum Versuch handeln, die in Estland nicht strafbar ist. Mangels Vollendungsvorsatzes kommt eine Strafbarkeit wegen Anstiftung in dieser Fallgestaltung also nicht in Betracht.

Es reicht aus, wenn der Vorsatz des Anstifters die wesentlichen Umstände der Haupttat umfasst und diese als konkretes und individualisierbares Ereignis betrachtet werden kann. Ein gemeinsamer Tatplan von Täter und Anstifter wird nicht gefordert.^{*69}

Die Fragen des *omnimodo facturus* werden vom Staatsgericht nicht im Zusammenhang mit der Anstiftung erörtert.^{*70} In der Lehre nimmt man an, dass in Fällen, in denen der künftige Täter zur Tatbegehung entschlossen ist, bevor die Handlung des Anstifters erfolgt, keine Anstiftung vorliegt. Da im estnischen Strafrecht eine versuchte Teilnahme nicht strafbar ist, kommt allenfalls eine Strafbarkeit wegen psychischer Beihilfe in Betracht. Strafbare Anstiftung kann hier jedoch insoweit vorliegen, als der schon generell zur Tat Entschlossene zu einer Änderung seines Tatplans veranlasst wird.

3.2.2. Beihilfe

Gehilfe ist derjenige, der dem Täter vorsätzlich bei der Begehung einer vorsätzlichen rechtswidrigen Tat Hilfe leistet (§ 22 III StGB). Damit unterstützt er nur die fremde Tat und beherrscht sie nicht.

Die Beihilfetat kann in drei Formen geleistet werden: physisch, materiell oder geistig (§ 22 III StGB). Während die erste und die dritte dieser Formen als die traditionellen bezeichnet werden (sogenannte Hilfe durch Rat und Tat), ist die materielle Beihilfe eine Unterart der physischen Beihilfe, die sich primär auf die finanzielle (estn. *aineline*) Unterstützung des Täters bezieht.^{*71}

Die Beihilfe muss zwar kausal für die Haupttat sein, aber es werden nicht zu strenge Anforderungen an die Kausalität gestellt. So ist es nicht erforderlich, dass ohne die Beihilfe die Haupttat überhaupt nicht möglich wäre. Es reicht völlig aus, wenn die geleistete Hilfe den Ablauf der Kausalkette positiv beeinflusst bzw. unterstützt, d.h. die Haupttat ohne die Handlung des Gehilfen wesentlich erschwert gewesen wäre.^{*72} Als Beihilfetat gilt auch solche, die im Rahmen des *omnimodo facturus* den beim Täter bereits vorhandenen Vorsatz unterstützt, bestärkt oder bestätigt.^{*73}

Auch wenn die Haupttat nicht ohne Beihilfe zustande gekommen wäre, bedeutet dies nicht, dass es sich in einem solchen Fall um Täterschaft handelt.^{*74} Es ist allerdings möglich, dass in der Gerichtspraxis die Grenzen zwischen Täterschaft (z.B. das Eindringen in ein Gebäude und die Wegnahme einer Sache beim Diebstahl) und Teilnahme (z.B. Wachestehen unter dem Fenster des Gebäudes) verschwimmen.^{*75} Damit bestünde aber die Gefahr, dass die Abstammung der Tatherrschaftstheorie von der formal-objektiven Theorie nicht mehr erkennbar wäre und die Mängel der subjektiven Theorie dahingehend übernommen würden, dass die notwendige Voraussetzung der Verwirklichung der Tatbestandsmerkmale durch den Täter nicht mehr erforderlich wäre.

Das frühere StGB enthielt als eine Form der Beihilfe das im Vorhinein dem Täter gegebene Versprechen, ihn zu verbergen oder die Tat zu verheimlichen (§ 17 VI StGB a.F.). Im geltenden StGB gibt es eine entsprechende Bestimmung nicht mehr, was aber nicht bedeutet, dass in einem solchen Fall keine Beihilfe vorliegt. Es handelt sich dabei um eine geistige Beihilfe.^{*76}

⁶⁸ Siehe ESG Nr. 3-1-1-15-01. – RT III 2001, 11, 16 (auf Estnisch); Nr. 3-1-1-110-04. – RT III 2004, 38, 384 (auf Estnisch). Kritisch zum letzten Urteil vgl. U. Lõhmus. Kuriteo matkimisest. Kas riik võib provotseerida kuritegu? (Über das künstliche Verbrechen. Darf der Staat ein Verbrechen provozieren?) – Juridica 2005/4, S. 223–230 (auf Estnisch).

⁶⁹ Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 5, 6.1; J. Sootak (Hinweis 22), S. 74 f. Einschlägige Entscheidungen des Staatsgerichts sind nicht bekannt.

⁷⁰ Bei der Figur des *omnimodo facturus* kann der Anstifter dann bestraft werden, wenn er bei einem bereits zur Tat entschlossenen Täter den Vorsatz zu einem gesonderten Tatteil hervorruft, der eine selbstständige strafrechtliche Bedeutung erlangen kann, z.B. zu einem Tatteil, der als selbstständiger Tatbestand oder als qualifizierter Tatbestand gelten kann. Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 6.1; J. Sootak (Hinweis 22), S. 72 ff. Einschlägige Entscheidungen des Staatsgerichts sind nicht bekannt.

⁷¹ Vgl. J. Sootak, P. Pikamäe (Hinweis 21), § 22 Komm. 9.4. In der Gerichtspraxis lassen sich gewisse Schwierigkeiten bei der Abgrenzung der genannten Beihilfeformen feststellen; einschlägige Entscheidungen des Staatsgerichts sind nicht bekannt.

⁷² Siehe ESG Nr. 3-1-1-60-02. – RT III 2002, 16, 191 (auf Estnisch); Nr. 3-1-1-69-02. – RT III 2002, 19, 217 (auf Estnisch); Nr. 3-1-1-94-00. – RT III 2000, 24, 261 (auf Estnisch).

⁷³ Siehe ESG Nr. 3-1-1-94-00. – RT III 2000, 24, 261 (auf Estnisch).

⁷⁴ Die genannten Figuren – Täterschaft und Teilnahme – unterscheiden sich aufgrund der Tatherrschaftstheorie darin, wer die Haupttat als Täter beherrscht und wer sie nur als Teilnehmer gefördert hat. Siehe ESG Nr. 3-1-1-98-97. – RT III 1999, 1, 1 (auf Estnisch); Nr. 3-1-1-97-04. – RT III 2005, 4, 36 (auf Estnisch).

⁷⁵ So hat das Staatsgericht im Rahmen eines *obiter dictum* als Beispiele für Mittäterschaft das Wachestehen oder das Ablenken der Aufmerksamkeit Dritter erwähnt. Siehe ESG Nr. 3-1-1-97-04. – RT III 2005, 4, 36 (auf Estnisch).

⁷⁶ Siehe ESG Nr. 3-1-1-60-02. – RT III 2002, 16, 191 (auf Estnisch).

Auf der subjektiven Seite des Gehilfen können alle drei Vorsatzformen vorliegen.^{*77} Der Gehilfe handelt nach Meinung des Staatsgerichts vorsätzlich, wenn er es für möglich hält, dass er eine fremde Tat unterstützt und der Erfolg mit Hilfe seines Beitrags auch dann eintritt, wenn er diesen nicht gebilligt oder für nicht wünschenswert gehalten hat.^{*78} Bezieht sich aber der Vorsatz des Gehilfen nicht auch auf einen weitergehenden Erfolg, sind die Handlungen, die zwar objektiv die Haupttat unterstützt haben könnten, nicht als Beihilfe zu qualifizieren.^{*79}

Im Urteilstenor sind ein Hinweis auf § 22 II StGB sowie die entsprechenden Paragraphen des BT erforderlich. Selbstverständlich ist auch eine Beihilfe möglich, die von mehreren, d.h. durch eine Gruppe begangen wird, was allerdings nicht aus § 22 II StGB hervorgeht.

Leistet jemand einer Gruppe Hilfe und gibt es bei im Haupttatbestand die Qualifikation der Begehung durch eine Gruppe^{*80}, weist man bei der Subsumtion der Tat des Gehilfen auch auf das entsprechende qualifizierende Merkmal hin. Das bedeutet, dass der Gehilfe als Teilnehmer am Gruppendedikt strafbar ist, obwohl er selbst nicht zu der Gruppe gehört.^{*81}

⁷⁷ ESG Nr. 3-1-1-28-02. – RT III 2002, 12, 129 (auf Estnisch); Nr. 3-1-1-69-02. – RT III 2002, 19, 217 (auf Estnisch).

⁷⁸ ESG Nr. 3-1-1-150-03. – RT III 2004, 5, 51 (auf Estnisch). Mehr wird dazu nicht ausgeführt; eine Abgrenzung zwischen dem bedingten Vorsatz und der bewussten Fahrlässigkeit nimmt das Staatsgericht nicht vor.

⁷⁹ Z.B. hatte in einem Fall T ein Opfer zunächst getreten und damit zwar den späteren Raub ermöglicht, aber nicht die spätere Tötung des Opfers durch M unterstützt, um so mehr, als T über den Tod des Opfers entsetzt war. Siehe ESG Nr. 3-1-1-69-02. – RT III 2002, 19, 217 (auf Estnisch).

⁸⁰ Z.B. § 200 II 7 StGB (Gruppenraub).

⁸¹ Siehe ESG Nr. 3-1-1-11-04. – RT III 2004, 8, 87 (auf Estnisch).



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Estonian Schoolchildren's Opinions about Violence and the Possibilities for Preventing It

1. Introduction

An individual's behaviour is largely dependent on whether and to what extent he or she acknowledges which code of conduct he or she pursues in his or her behaviour; the acknowledgement of rules, in turn, determines the attitude of the individual towards the phenomena currently affecting our life in society at a particular moment.

A phenomenon that has become an inseparable part of our daily life is violence that can be expressed in very different forms — as school and domestic violence, violence against children and animals, etc. As a rule, violence is defined as behaviour that causes or may cause bodily injuries. However, violence can be defined in a broader basis as well, by including in the definition both physical and psychological damage along with indifference to or disregard for others' needs.

Violence is a phenomenon that characterises society as a whole, and embraces certain gender specificity. While men experience violence mostly in public places and the offender is predominantly an unfamiliar person, women fall victims to violence most often in their family and the offender is the woman's partner. Statistically, home is the most unsafe place for a woman. According to a survey of the Open Society Institute, 285*¹ women fall victim to physical or sexual violence in Estonia every day and 2/3 of these cases take place at home. Also, 227 men experience violence every day, but only 9% of the cases take place in their homes.*²

In addition to adults, violence (including sexual violence) also affects youth (schoolchildren) daily. A survey of sexual abuse, conducted in 1999, revealed that 70% of the responding children had experienced sexual abuse (including mild and severe verbal abuse, mental abuse, physical and severe physical sexual abuse).^{*3} When we

¹ The size of the Estonian population was 1,340,935 as of 1 January 2008. Source: <http://www.stat.ee/pohinaitajad> (11.09.2008) (in Estonian).

² Võrdsed võimalused inimväärses eluks. Sotsiaalministeerium. Vägivald (Equal Opportunities for Decent Life. Ministry of Social Affairs. Violence). Available at <http://www.sm.ee/esttxt/pages/goproweb0908> (31.10.2006) (in Estonian).

³ Võrdsed võimalused inimväärses eluks. Sotsiaalministeerium. Koolivägivalda või seksuaalse väärkohtlemise all kannatavad lapsed (Equal Opportunities for Decent Life. Ministry of Social Affairs. Children Experiencing School Violence or Sexual Abuse). Available at <http://www.sm.ee/esttxt/pages/goproweb0484> (31.10.2006) (in Estonian).

Violence is not characteristic of a secure society; yet the attitude of the members of society towards violence characterises, to a great extent, the level of their legal conscience. Awareness of the violence problem (especially among young people) as well as searching for and identifying measures to reduce it gives a bigger contribution to increasing the security of society. One of the factors, the importance of which both in developing (legal) conscience and reducing violence cannot be overestimated, is social control, which applies both to self-control as well as informal and formal control. Social control, as an evaluation system, shapes public opinion which may play a considerably greater role in social life and a form of social behaviour, than it may seem at the first glance.

Conscience serves as an internal moral voice, the core of justice, a so-called regulatory filter. With a clear conscience, a person is satisfied because the feeling of solidarity serves as an act of self-realisation in an ideal community. If this regulatory filter detects a deviation from the standards accepted on the level of consciousness, this elicits fear that is manifested as an accusing reaction in the form of self-criticism and punishment.

⁸ D. Goleman. Töö emotsionaalse intelligentsusega. Emotsionaalse intelligentsuse kasutamine (Working with Emotional Intelligence. Use of Emotional Intelligence). Tallinn 2001, p. 101 (in Estonian).

Consciousness stems from the understanding that an individual has a responsibility and liability to other people, which constitutes the individual's responsibility and liability to himself or herself. Unlike shame, consciousness does not depend on the opinion of others and in this sense serves as an internal moral judge. An advanced consciousness signals a morally mature personality. People who act in a manner that is acceptable to society can be divided into (1) people who are mostly guided by consciousness in their behaviour (shame plays an insignificant part), and (2) people who are guided by shame (consciousness remains secondary). The former are undoubtedly morally more mature.^{*9}

Figuratively, consciousness has been compared to a sharp rock that is located in the soul of an individual. If the individual does not behave as required, the rock starts to roll and hurts the soul. But rolling wears down the edges of the rock and the more the rock rolls, the less it hurts the soul. This means that consciousness no longer responds.^{*10} In cases like that, the individual no longer pays critical attention to any behaviour that is contrary to the standards, including offences.

In this way, we can view crime control policy in a wider social context because the core values of society are protected through that. Aimed directly at criminal behaviour, by controlling crime, a certain social and cultural environment is reproduced and social capital (condemnation, punishment as a response to the violation of generally accepted standards, remedy of damage caused by crime) is created.^{*11}

3. Crime and violence in society

The practice of crime and violence control is inseparably related to the development level and cultural space of a particular society. This necessitates consideration of the problems that society faces at a particular moment when drafting the criminal policy of a country.

When implementing criminal policy, it is important to know how safe the surrounding environment appears to the population and what measures the population consider appropriate and efficient in increasing the safety of society. Hence, the decision of the *Riigikogu* of 21 October 2003 emphasises that relating to criminal policy, the 'approved development trends must also be observed when planning means to fight crime and [...] local governments, citizens' associations and individuals must be involved in preventing offence more than before'.^{*12} Here we cannot underestimate the youngest members of our society — children — whose attitudes, understanding and evaluations reflect the perceptions of adults and determine how violent, criminal or, *vice versa*, law abiding our future society will be.

The level of juvenile delinquency has been high in Estonia over the years: 255 offences committed by persons aged under 16 in 2002, while the number was 190 in 2003 and 492 in 2004; the number of offences committed by young people aged from 16 to 17 was 688, 705 and 923, respectively; the number of offences committed by people aged from 18 to 24 was 3438, 3594 and 4222, respectively.^{*13}

When analysing the offences committed by minors in 2007 by categories, it appears that one-half of the offences committed by minors in 2007 were against property, offences against public order constituted one-fifth and offences against the person accounted for 13%. During that year, 8 killers and rapists who were minors were identified; the number of robberies committed by minors was 150. Offences against public trust made up 9%. The latter comprised, in most cases, the misuse of an important identity document, that is, by using documents that did not belong to them, young people attempted to attend various events or enter night clubs, for which they did not have permission because of their age. We may presume that a considerable part of these offences were committed out of foolishness. Hence, both national institutions and local governments can take preventive steps to spare, on the one hand, young people of the proceedings, and on the other hand, reserve resources for fighting more serious offences.^{*14}

⁹ I. Meos. *Filosoofia sõnaraamat. Olulisi mõisteid, koolkondi, filosoofe, seisukohti* (Dictionary of Philosophy. Important Notions, Schools, Philosophers, Opinions). Tallinn 2002, p. 239.

¹⁰ *Ibid.*

¹¹ Eesti inimarengu aruanne 2001: 2.4. Karistuspoliitika Eestis 1991–2000 (Estonian human development report 2001. Punishment policy in Estonia 1991–2000). Available at <http://72.14.203.104/search?q=cache:D2E2PI2tMZgJ:www.iiss.ee/nhdr/2001/2.4.html> (28.03.2007) (in Estonian).

¹² Kriminaalpoliitika arengusuundade aastani 2010 heakskiitmine. Riigikogu 21. oktoobri 2003. a otsus (Approval of development trends of criminal policy until 2010. Decision of the Riigikogu of 21 October 2003). Available at <https://www.riigiteataja.ee/ert/act.jsp?id=637829> (4.04.2007) (in Estonian).

¹³ Kuritegudes süüdistatavad. Isikute rühm ning aasta (People Accused of Crimes. Group of People and Year). Available at <http://pub.stat.ee/px-web.2001/Dialog/Saveshow.asp> (3.10.2006) (in Estonian).

¹⁴ Speech by Minister of Justice Rein Lang at the prosecutors' general assembly on 4.04.2008 (Note 4).

In addition to crimes, minors commit various misdemeanours and offences. The results of a survey conducted among ordinary schoolchildren in different districts in Estonia in 2006, showed that the majority of them had violated the law at least once during the previous year. According to the survey, pupils aged from 11 to 15 had committed the following offences^{*15}:

	Boys	Girls
Shouting in a public place	33%	27%
Present in an intoxicated state in a public place	19%	4%
Damaged or destroyed property belonging to strangers	19%	8%
Participated in gang fights	19%	5%
Throwing rocks or bottles at people	16%	7%
Theft of items with a value less than EEK 50	14%	51%
Rape or attempted rape	1%	0%

Thus, minors and young people unavoidably 'contribute' to the decreasing security of society and provide a new generation of adult criminals. This gives rise to the question of what minors themselves think about crime and violence and what would be the possibilities of ensuring security for themselves and society.

4. Schoolchildren of Tartu on violence and its prevention

Violence (just as crime) is an eternal phenomenon that exists in any society. The forms of violence change in line with the development of society and/or political processes; in certain cases, the degree of cruelty, intensity and frequency also changes (*cf.* during war and peace) but the human mind recognises, regardless of the processes described, what acts are violent and a person always searches for opportunities to counter violence. This represents the realisation of the core of Superego (which develops most rapidly at the ages of 5 and 6, then during adolescence when a person starts to make more conscious decisions, values and ideals are adopted), when the already fixed values and ideals can no longer be changed or always even identified. Thus, an individual does not always recognise why he or she feels guilty or disturbed. He or she fails to perceive that he or she has violated a rule accepted during childhood, the meaning of which he or she has already forgotten.^{*16} The perception of violence is therefore more static by nature than the changes in the content and/or character of acts of violence accompanying the development of society. This fact allows, in the opinion of the author, for an analysis to be performed in this paper on the survey conducted in 2003.

Within the framework of an international survey in 2003^{*17} we questioned Tartu schoolchildren^{*18}, to find out how violent or criminal they considered our society and what they had done to increase their security.

The responses to questions 'How has violence changed among the youth over the past couple of years?' are depicted in Figures 1 and 2. The answers given to that question were given on a five-point scale: 5 – decreased significantly, 4 – decreased to some extent, 3 – no change, 2 – increased to some extent, and 1 – increased significantly. Since the survey was carried out in the winter and spring of 2003, the phrase 'over the last couple of years' means that the pupils had to look back to 2001. On the following scale, the higher mean indicates trends of decreasing violence according to pupils and the smaller mean, on the contrary, the increasing of violence.

¹⁵ A. Kuus. Suur osa teismelistest on seadust rikkunud (Large Share of Young People Have Violated the Law). – Postimees, 31.08.2006 (in Estonian).

¹⁶ L. Keltikangas-Järvinen. Agressiivne laps. Kuidas suunata lapse isiksuse arengut (Aggressive Child. How to Direct the Development of the Child's Personality). Tallinn 1992, p. 41 (in Estonian).

¹⁷ Youth's Experience of Violence as Accused and Victim in International Project Baltic Sea: European Future Region in 2002–2004. Project Manager in Estonia Prof. J. Sootak, co-ordinator University of Greifswald.

¹⁸ The respondents were pupils of Forms 8 and 9 of Estonian and Russian basic schools and freshmen of vocational schools in Tartu. (The sample was comprised of 363 pupils, including 200 boys and 163 girls; the average age of pupils was 15–16 years). Tartu is the second largest town in Estonia and the centre of Southern Estonia. The population of Tartu exceeded 100,000 in 1977 and has remained around that level to date. According to the population register, as of 1 August 2007, the number of people who had registered Tartu as their residence was 101,250. Of them, 80% are Estonians, 16% are Russians and 4% represent other nations.

Figure 1. Opinions of young people on changes in violence over the past two years, depending on the gender of pupils (mean values).^{*19}

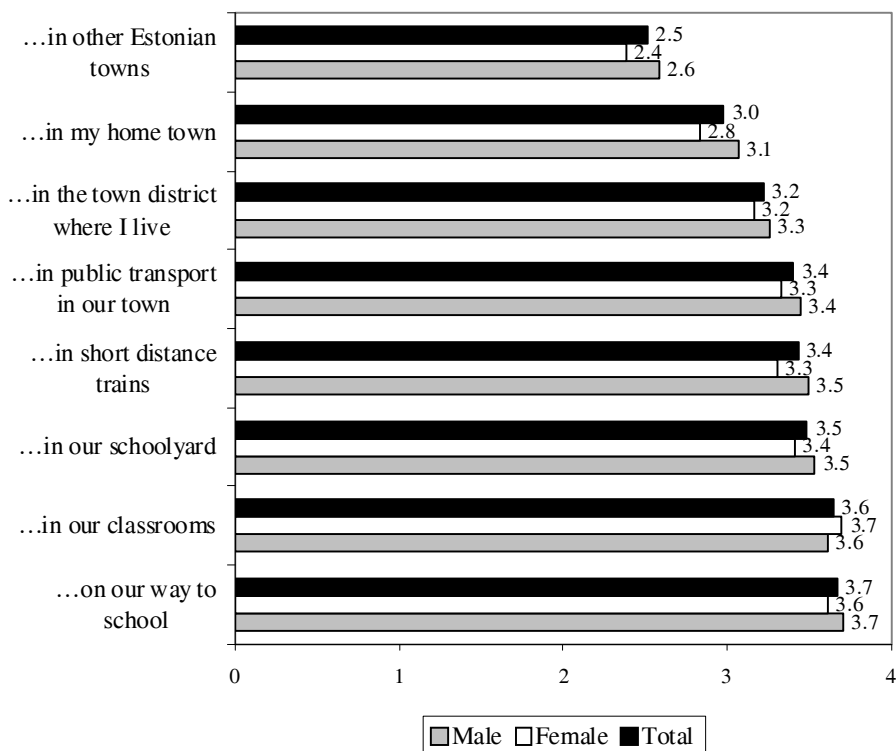
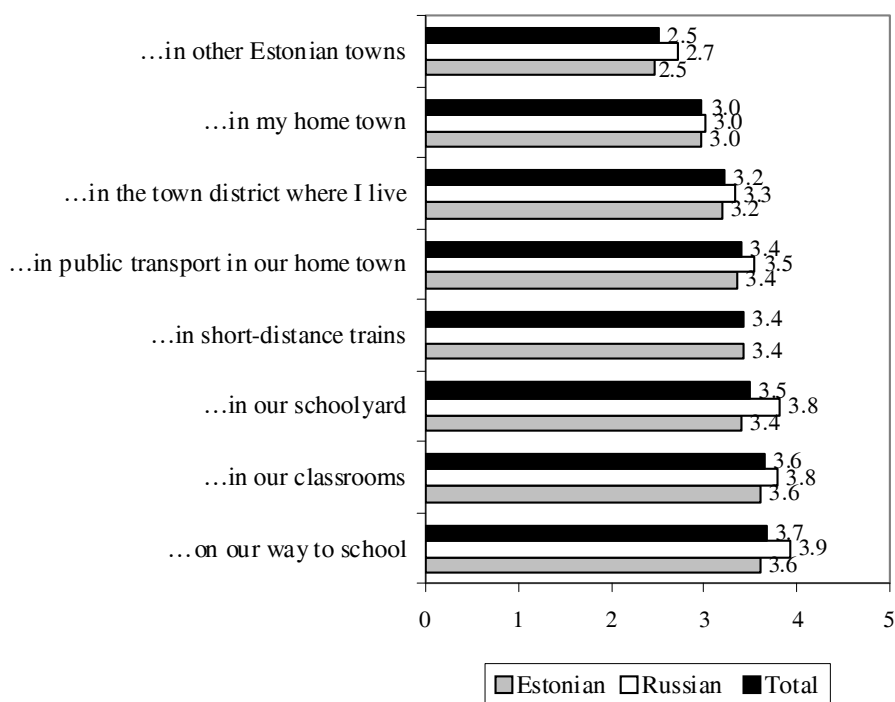


Figure 2. Opinions of young people on changes in violence over the past two years, depending on the gender of pupils (mean values).



¹⁹ All the results of the survey included in this paper have been presented as arithmetic means.

The comparison of the data given in the figures allows for the conclusion to be made that the results differ most in relation to national background (see Figure 2). The opinions of pupils speaking different languages differ most regarding classroom and schoolyard violence. There are considerably fewer Russian-speaking pupils, compared to Estonian youth, who think that the level of violence has remained the same. The pupils who opine that school violence has decreased over the years outnumber those who do not. This may be caused, among other things, by the increasingly serious attitude of Russian-speaking pupils towards education, which is the most important guarantee for integration into our society. The decreasing violence in Russian basic schools may also be ascribed to stricter discipline and order compared with Estonian schools, as well as to the peculiarities of Slavic culture and national feelings of togetherness.

It is noteworthy that regardless of the language and the gender of the respondents (see Figure 1), the other towns apart from their own home town have a higher rate of violence. Such an opinion implies that the youth are aware of the acts of violence registered in our society but since they have not fallen victims to violence in their home town, they do not perceive their home town to be as violent as the other towns. Due to media coverage, just as adults, the youth have also developed certain stereotypical preconceptions about certain regions of Estonia (above all the capital Tallinn and East-Viru County²⁰), as if more acts of violence were registered there than in other Estonian towns, so smaller towns and more 'peaceful' areas leave the impression of being less violent.

When looking at the number of offences registered in Estonia and the areas where they were committed, we see that the following number of offences has been committed in Tallinn: 25,587 in 2002; 25,026 in 2003; 24,393 in 2004, and 24,584 in 2005; in East-Viru County, the indicators were 5652, 6518, 6318 and 6412, respectively. Considering the number of offences registered in Tartu County over the same period, we may spot a growing trend: in 2002, the number of offences registered in the county was 4285, while 4352 offences were registered in 2003, and 4388 in 2004, complemented by 4480 offences in 2005.²¹ It is possible to fall victim to an offence in any region in Estonia. In their opinion, young people proceeded from the stereotypical preconceptions or their personal experience of violence.

As may be expected, young people feel safe²² during the daytime in an environment familiar to them (streets, public transport, school); their feeling of security is not that strong when staying at various places of the town in the evening or at night. Hence, the responses given here are in line with those analysed above, which suggested that pupils consider that violence has decreased at school and around it over the previous years.

When boys and girls feel equally safe during the daytime, insecurity generally increases with darkness — people's sense of danger rises regardless of their gender. Girls feel especially insecure and particularly in places where young people tend to gather in groups. This gives rise to the question what to do and what pupils have done so far to protect themselves or others from violence.

It appears from the survey that the most frequently used option is, for example, to carry a mobile phone to call for help ($x = 2.8$) and the cases of possession of some kind of a weapon are most rare ($x = 4.8 \dots 4.9$). The survey actually reveals that 51% of the respondents often or very often carry along something to call for help, and only 2.5% of the respondents carry often or very often some type of a weapon (e.g., gas weapon). This is never done by 94% of the respondents, i.e., they do not have a weapon.

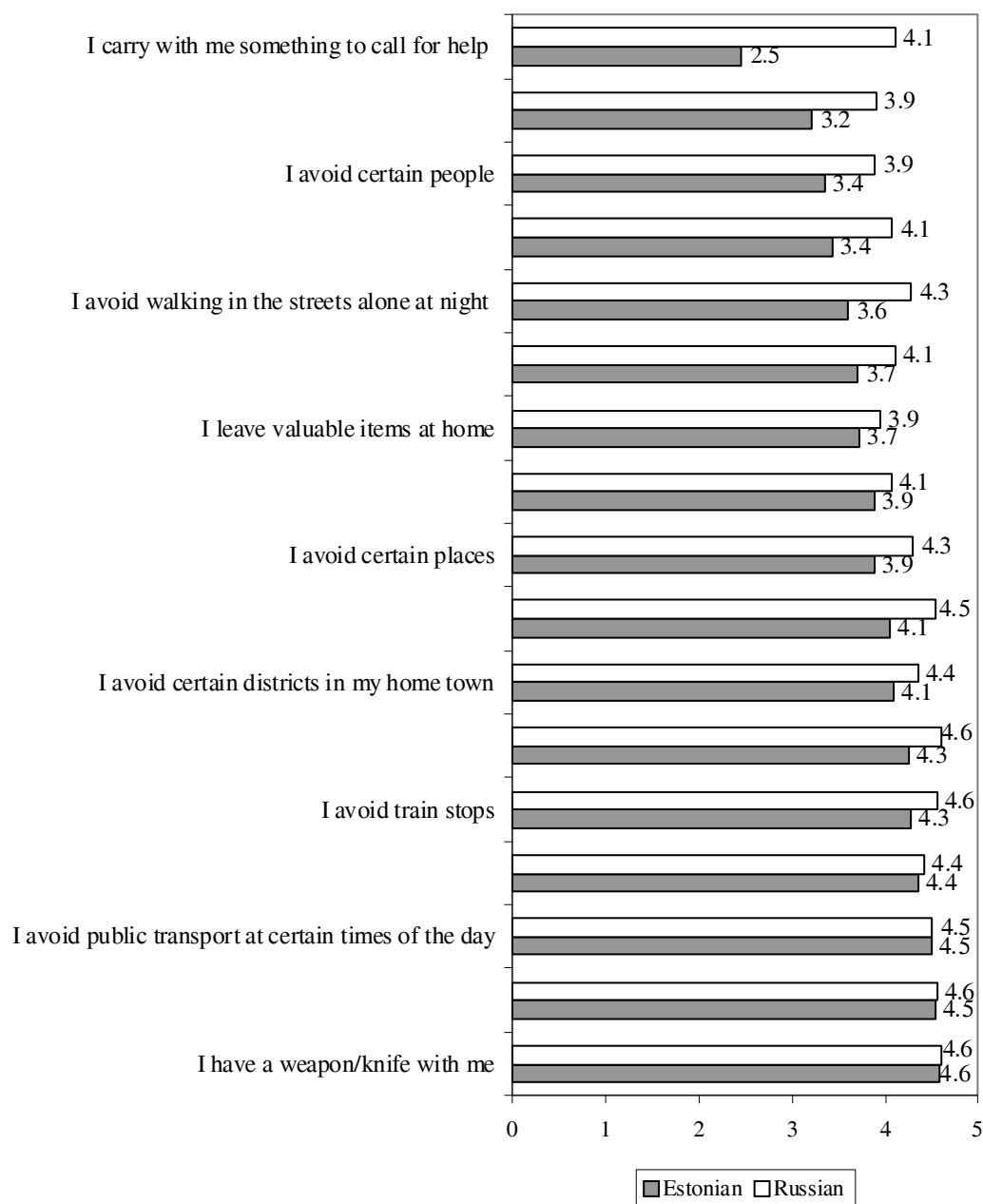
The results of the survey indicate that many young people do not avoid carrying with them large amounts of money ($x = 3.4$) and valuable items ($x = 3.8$), or avoid certain places (dark parks, passageways, etc.) or certain people. They probably rely too much on the possibility to call for help, without thinking that it may not always be possible. This certainly relates to the personal experience of young people — unless they have fallen victim to offences, they cannot be fearful.

Major differences appear between the answers given to this question by Estonian- and Russian-speaking pupils (see Figure 3).

²⁰ East-Viru County is a traditional industrial region in Estonia, which was dominated by the oil shale industry during the Soviet period, and where the work force largely consisted of migrants to Estonia. The migration that lasted for decades in East-Viru County rendered Estonians a national minority. The industrial development that was based on mineral resources resulted in a unidirectional economy, due to which the social environment is monotonous. Now that several of the mines have been closed down, the region suffers from unemployment, one of the important causes of which is the poor or non-existent knowledge of Estonian as the official language of the Republic of Estonia. A large proportion of migrants and their descendants, and unemployment, are the main factors that have shaped the stereotype that the East-Viru County is more violent and criminal than the other regions in Estonia.

²¹ Registreeritud kuriteod. Aasta, kuriteo toimepaneku paik ning näitaja (Registered Crimes. Year, Place Committed, Crime and Indicator). Available at <http://pub.stat.ee/px-web.2001/Dialog/Saveshow.asp> (3.10.2006) (in Estonian).

²² The question 'How safe do you feel at the following places?' could be answered on a four-point scale: 4 – very unsafe, 3 – unsafe, 2 – safe, and 1 – very safe.

Figure 3. Evaluation of various ways of conduct (mean values)*²³

The general trend is that Estonian pupils prefer more often all the ways of action offered in the questionnaire compared to their Russian peers. If according to the pupils of Estonian basic schools, the most efficient method of protecting themselves and if necessary also other people was the opportunity to call for help (e.g., by a mobile phone), Russian-speaking young people considered leaving large amounts of money and valuable items at home as well as avoiding certain people to be most efficient. The opportunity to call for help (e.g., by carrying a mobile phone) was surprisingly unpopular among Russian-speaking respondents. When comparing the two groups, it appears significant that Russian-speaking pupils did not rely on any of the options offered by us, which would help reduce the danger of falling victim to violence. It is possible that none of the ways of conduct suggested by us seemed very efficient to them; it is, however, also possible that non-Estonians, above all, rely on themselves in the case of the danger of violence and believe that they would find a way out

²³ Twenty-two ways of conduct were presented to pupils to prevent violence or to protect others from it. Pupils' opinions were measured on a five-point scale: 5 – never, 4 – seldom, 3 – sometimes, 2 – often, and 1 – very often. To give an integral overview, we have to use arithmetic means. The following was taken into account when interpreting the mean values: the smaller the numerical value of the mean, the more frequently the respondent takes action to prevent violence. The higher the mean, the less often relevant action is taken.

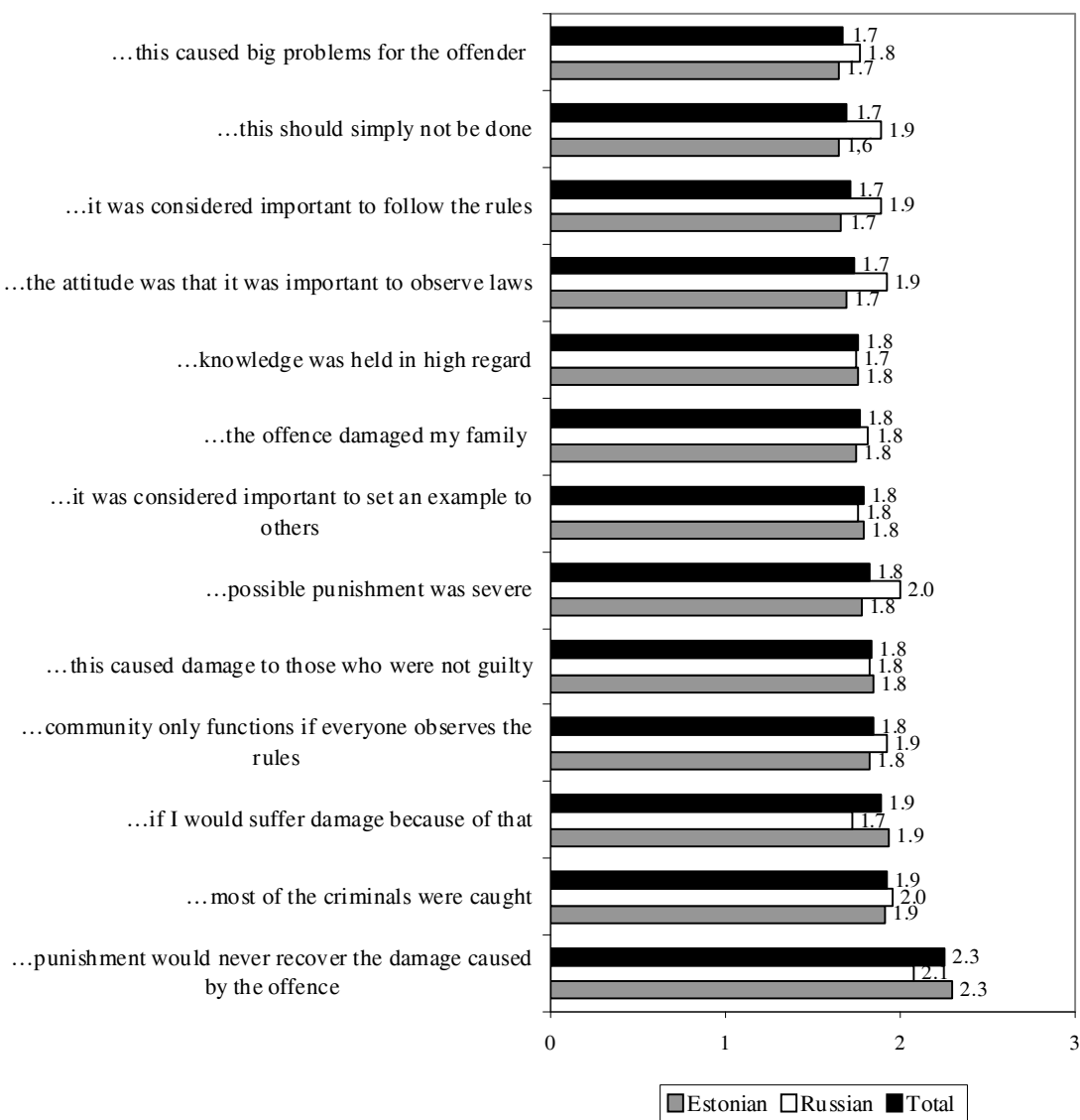
themselves in a critical situation (e.g., avoid remaining in isolated places in the dark, rely on their physical strength when it would be necessary to resist an attack, etc.).

The data at our disposal does not allow us to provide an unequivocal explanation of the reasons for different patterns of action based on national background. We cannot confirm here whether it is a lower sensibility threshold for Russian-speaking children that does not regard as dangerous situations in which Estonian pupils already take precautions, or the reason lies somewhere in the socioeconomic or cultural and everyday field.

As said above, we can all do something to prevent violence and crime. The problem has, however, a so-called national aspect, in which the drafted and adopted laws must be appropriate to fight the vices both as regards prevention and punishment of those who are guilty. What would be the reasons, according to our young people, why it would be reasonable to refrain from committing an offence? Would this serve as a point of departure for the legislator as well?

In the survey, the following statement was presented to pupils: 'It would be more reasonable not to commit an offence if ...' The responses to the statements given in Figure 4 were provided using a four-point scale: 4 – completely disagree, 3 – disagree, 2 – agree rather than disagree, and 1 – completely agree. Thus, the smaller the numerical value of the mean, the more respondents agree with the statement, and *vice versa*, the bigger the numerical value, the smaller the number of respondents who agreed. The response options have been given in shortened versions in the Figure.

Figure 4. Responses broken down by language (mean values)



The results allow for the conclusion to be reached that, according to the pupils, it would be reasonable to refrain from committing an offence if this caused big problems for the offender; they also valued the upswing of legal consciousness among the population (e.g., they considered it important to follow the rules, value knowledge, consider it important to set a good example to others). At the same time, the respondents did not find that severe punishments would affect the reasonability of committing an offence.

5. Conclusions

The 'new' Estonian society, the building of which immediately followed the restoration of Estonian independence in 1991 and gained momentum after the membership of the European Union in 2004, has to date developed into a society in which we have priorities for future development and a vision of what our country and society could look like in the future. Our development priorities certainly include movement towards a more secure society, while reduction of violence in society and involvement of society as a whole in achieving the goal would contribute to that.

Unfortunately, Estonian society as a whole cannot be considered safe yet — there is too much violence around us, and the 'number of offences committed by minors and directed at them' is high.^{*24}

According to schoolchildren living in Tartu, an increase in violence may be spotted in other Estonian towns rather than their home town over the past few years. This can be explained predominantly by stereotypical preconceptions developed by the media that certain Estonian regions (e.g., in East-Viru County) are more violent and criminal than the other Estonian regions. At the same time, violence (including school violence) serves as a phenomenon that has touched upon all Estonian regions more or less. As appears from Figures 1 and 2, the respondents claimed that violence in their schoolyard and school house had decreased over the previous years. However, looking at the relevant statistics and the results of the surveys (see, e.g., the sources indicated in the introductory part of this paper), there is no reason for excessive optimism. A large number of cases of school violence provide evidence of low self-control both in the relationships between minors and in relationships involving a minor and an adult (pupil and teacher). In the case of minors, it is a great concern that young people do not often even realise that their act has been violent.^{*25} This, once again, signals an urgent need for society (and the state!) to develop the legal consciousness of young people in order to cultivate a healthy attitude to the surrounding environment and clarify the limits between justified and unjustified behaviour.

One of the possibilities to limit violence is to use (formal social control) measures (as efficiently as possible!) applied by the state against individuals who have resorted to violence and committed offences. According to the schoolchildren involved in the study, it is reasonable to refrain from committing an offence if this would cause great problems for the offender and his or her family; they also value an upswing in the legal consciousness among the population. At the same time, the respondents do not find that severe punishments could affect the reasonability of committing an offence (see Figure 4).

Once again, this testifies that it is more important that severe punishments strive for changing people's attitude in the broadest sense of the word — starting from their attitude toward themselves to their attitude towards all other living creatures, nature and unwritten and written rules.

The survey conducted confirms, on the one hand, the need to identify and apply more efficiently measures to increase legal consciousness, and on the other hand, it is unavoidable to consider what would be the most efficient methods of social control in the present society.

²⁴ See speech by Minister of Justice Rein Lang at the prosecutors' general assembly on 4.04.2008 (Note 4).

²⁵ See, e.g., A. Kuus. Teismeliste korteripidu lõppes kassi tapmisega (An Adolescent House Party Ended in the Killing of a Cat). Postimees, 28.03.2007 (in Estonian).



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The Siege of the Estonian Embassy in Moscow: Protection of a Diplomatic Mission and Its Staff in the Receiving State

1. Introduction

States establish diplomatic missions and send both diplomatic and non-diplomatic staff abroad in order to represent and protect their interests and those of their nationals. Such missions and personnel are granted different privileges and immunities in the receiving states so that they can perform their official functions as independently and efficiently as possible. These guarantees are supposed to prevent attacks on diplomatic missions and their staff by both public officials and private persons and are intended to avoid any other obstacles to performance of their official functions. In reality, there is not often need for such a protection — states refrain from interfering, as they are interested in mutually friendly relations and wish their own diplomatic missions and the staff thereof to have the widest possible freedom to operate in the respective receiving states. The principle of reciprocity is the most effective means against breaches of diplomatic law. Nevertheless, there are still occasions on which the privileges and immunities provided become indispensable to ensuring the normal functioning of a diplomatic mission and the physical safety of its staff. The danger may originate from local authorities as well as from private persons or their groups, acting independently or under the order of the receiving state. Sometimes the receiving state chooses to ignore completely its obligations and allows the threatening situation to continue. The Estonian embassy in Moscow, which was subjected to threats, attacks, and blockade from 27 April to 5 May 2007, serves as an excellent example in this context. The incident in question illustrated that Russia sometimes displays a rather unusual understanding of the content and meaning of diplomatic privileges and immunities and of the obligations of the receiving state where the protection of a diplomatic mission and its staff is concerned. That incident was hardly an everyday happening; it will more likely serve in future textbooks as an example of flagrant breaches of diplomatic law. The present article discusses the nature and scope of the protection of the diplomatic mission and its staff and the obligations of the receiving state in ensuring such protection. Attention is focused on aspects of physical protection (obviously lacking in this incident), leaving aside judicial immunity and other privileges guaranteeing freedom of action. The article assesses the events in the vicinity of the Estonian embassy in Moscow in the light of diplomatic law as well as that of state and court practice.

2. Background

The siege began because the Estonian government decided to move a problematic war memorial from the middle of Tallinn. The Bronze Soldier has a turbulent and contradictory history. It was originally erected to honour Soviet soldiers who had 'liberated' Tallinn and fallen in the Great Patriotic War against Nazi Germany. The Soviet theme was revised when Estonia regained its independence; the monument was dedicated to all those who had fallen in the Second World War.

After Estonia regained independence, the monument did not receive much attention. However, in more recent years, the Bronze Soldier had gained significant symbolic value for the local Russian community of post-war immigrants, symbolising the Soviet victory over Nazi Germany and their claim to rights in Estonia. By contrast, Estonians considered the monument to be a symbol of the Soviet annexation and its repressive regime. Since 2006, several intense quarrels (although not violent) took place between Estonians and Russians around the Bronze Soldier. There were strong calls to remove the Soviet monument from the middle of the capital of Estonia. The positions of the Estonian and Russian communities on the question were sharply divided. Finally, in April 2007, the Estonian government started preparations to exhume the remains of the Soviet soldiers buried under the monument and to rebury them in a more fitting place (because of the surface design, people were walking on the unmarked graves) and also to relocate the monument itself to the cemetery of the Estonian Defence Forces. The police surrounded the area on 26 April. The disagreement over these activities led to two-day massive protests, riots, and looting — the worst Estonia has ever seen — mostly by ethnic Russians. In the wake of these and related events, the Estonian government decided to remove the monument immediately, in contrast to the more methodical approach originally intended. The Bronze Soldier with its accompanying stone wall was removed on 27 April and the monument re-erected on 30 April (the stone wall was rebuilt later). DNA profiles were taken from exhumed remains and handed over to the Russian embassy so that relatives could reclaim the remains and rebury them elsewhere. Relatives claimed four sets of remains. Unclaimed remains were reburied at the military cemetery close to the Bronze Soldier.

As a protest, several youth organisations staged a virtual siege on the Estonian embassy in Moscow. For nine days, the protestors disturbed the peace of the embassy, prevented staff and visitors from entering or leaving the embassy, and physically attacked the embassy and the ambassador. The flagrant breaches of diplomatic law were possible on account of the toleration of these acts by the Russian authorities.

3. Different aspects of physical protection

According to long-established and universally recognised practice, receiving states must guarantee certain privileges and immunities to the diplomatic missions established in their territories and to diplomatic and non-diplomatic staff sent there. Such privileges and immunities are codified in the Vienna Convention on Diplomatic Relations (1961).¹ It stresses that the purpose of these privileges and immunities is not to benefit individuals but to ensure the efficient performance of the functions of diplomatic missions representing states.² Indeed, if a diplomatic mission and its staff were subject to the jurisdiction of the receiving state in the same manner as everyone else and therefore completely dependent on its goodwill, their actions potentially would be influenced to such an extent that the performance of the functions entrusted to them by the sending state is hampered. However, the privileges and immunities are necessary not only when the staff is exercising official functions but also, at least to some extent, in regard of their private actions, as the receiving state can influence their independence equally through their private life. For a similar reason, family members are considered an extension of a member of diplomatic or non-diplomatic staff and must also be protected.³

From the perspective of physical protection, there are three important guarantees:

1. Inviolability of the premises
2. Personal inviolability
3. Freedom of movement

¹ Vienna Convention on Diplomatic Relations, 18.04.1961, entered into force on 24.04.1964, 500 UNTS 95 (hereinafter: the Vienna Convention).

² *Ibid.*, preamble.

³ See Article 37 (1)–(3) of the Vienna Convention. The family members enjoy the same privileges and immunities as the respective member of diplomatic or non-diplomatic staff with the exception of the family members of a member of service staff who do not enjoy any privileges and immunities.

The first two of these were considered so important by the signatory states that the Vienna Convention does not include any exceptions from these inviolabilities.⁴ They constitute basic norms that are respected by all civilised nations and that rarely are violated; even when they are violated, the problem stems from extreme circumstances or, at worst, unawareness on the part of the actor concerned or the responsible person. The International Court of Justice has emphasised in the *Teheran* case that such obligations “are not merely contractual obligations [under the Vienna Convention], but also obligations under general international law”.⁵

3.1. Inviolability of the premises

The inviolability of the premises is an undeniably established norm of international law according to which the premises of a diplomatic mission physically present in the territory of the receiving state are not subject to the jurisdiction of the receiving state in the same manner as other property is.⁶ In the present context, there are two important aspects of inviolability of the premises: 1) the agents of the receiving state may not enter the premises of the mission, except with the consent of the head of the mission⁷, and 2) the receiving state has a special duty to take all appropriate steps to protect the premises of the mission against any intrusion or damage and to prevent any disturbance of the peace of the mission or impairment of its dignity.⁸

3.1.1. Prohibition to enter the premises of the mission

The prohibition from entering the premises of the mission imposes a negative obligation — to refrain from corresponding action. The inviolability of the premises is absolute, meaning that the premises of the mission may not be entered even by the police chasing a criminal or by fire-fighters if there is a fire on the premises of the mission. Entry is not even allowed if the receiving state has serious reason to believe that the premises of the mission are being used in a manner incompatible with the functions of the mission.⁹ For example, if the premises of the mission are used for smuggling weapons or narcotics or for organising terrorist attacks, the receiving state may merely ask for the assistance of the sending state to stop such activities occurring at its diplomatic mission. The first draft of the Vienna Convention included a right of the receiving state to enter the premises of a mission in cases of extreme emergency in order to eliminate serious threat to human lives, public health, or property or to defend the national security of the receiving state. This proposed text was eventually left out, as there was very little supporting state practice and allowing such a right would be likely to cause more problems than would denying it.¹⁰ Indeed, if it had been adopted, a malicious receiving state could simply have created a situation that would then justify entry to the premises of the mission. For instance, it is, on the one hand, very easy to claim that the national security of the receiving state necessitates entry while, on the other hand, it is very difficult to prove the contrary. Moreover, the practice should be that the head of the mission weighs the specific circumstances carefully when deciding whether to allow entry. There have been a number of example cases in which the head of a mission has denied entry in the circumstances mentioned above. Spain broke off diplomatic relations with Guatemala in February 1980 after the police entered the premises of the mission in order to free them from the peasants who had taken the ambassador and several other staff of the mission hostage, even though the head of the mission had refused them entry.¹¹

Perhaps the most drastic example concerns the April 1984 shooting incident surrounding the Libyan People's Bureau (Libya's preferred term for an embassy). The opponents of Colonel Qaddafi's regime had for some time already been holding regular protests in front of the Libyan mission. The day before a planned demonstration, Libyan diplomats requested the British authorities to prevent the demonstrations and also warned that they would otherwise not be responsible for the consequences. On the day of the demonstration, 17 April, someone opened fire on the protestors from the premises of the mission. As a consequence, several of them

⁴ The International Court of Justice has stated that “the principle of the inviolability of the persons of diplomatic agents and the premises of diplomatic missions is one of the very foundations of this long-established regime” of diplomatic law. *United States Diplomatic and Consular Staff in Teheran (United States of America v. Iran)*, Judgment. — ICJ Reports 1980 (3), paragraph 86.

⁵ *Ibid.*, paragraph 62.

⁶ The inviolability of the premises of the mission was originally derived from the personal inviolability of the head of the mission, but during the drafting process of the Vienna Convention, the International Law Commission formulated a new position that such inviolability is instead an attribute of the sovereignty of the sending state by reason of the fact that the premises are used as the headquarters of its mission. See *Yearbook of the International Law Commission*. Vol. II. New York: United Nations 1958, p. 95.

⁷ Article 22 (1) of the Vienna Convention.

⁸ Article 22 (2) of the Vienna Convention.

⁹ Article 41 (3) of the Vienna Convention prohibits the use of the premises of the mission in any manner incompatible with the functions of the mission as laid down in the Vienna Convention or by other rules of general international law or by any special agreements in force between the sending and receiving state.

¹⁰ *Yearbook of the International Law Commission*. Vol. I. New York: United Nations 1957, p. 56.

¹¹ B. Sen. A Diplomat's Handbook of International Law and Practice. 3rd revised edition. Dordrecht: Martinus Nijhoff 1988, p. 113.

were seriously injured and a female constable protecting the mission was killed. The police did not return fire, but the Libyan authorities in Tripoli were immediately asked to instruct those inside the mission to leave the building and to allow the premises to be searched by the police for weapons and explosives. Unsurprisingly, the request was refused. Instead, the British embassy in Tripoli was the scene of hostile demonstrations and some British nationals were unjustifiably arrested. The United Kingdom did not breach the inviolability of the mission, although such a possibility was considered (self-defence was mentioned as a potential justification). However, it was concluded finally that, according to the meaning and *travaux préparatoires* of Article 22, the premises of the mission do not lose inviolability in the event of inappropriate use of the premises and therefore it was necessary to utilise other measures.^{*12} As the parties were not able to settle their dispute, the United Kingdom (after some further violent acts) terminated diplomatic relations and ordered all members of the Libyan People's Bureau to leave by the end of April. The British authorities then entered the premises, in the presence of a representative of the Saudi Arabian embassy, and found weapons and relevant forensic evidence.^{*13}

This prohibition was not breached in the case of the Estonian embassy in Moscow. Entry by the Russian authorities to the premises of the mission would have been an obvious and very serious breach of the Vienna Convention that cannot be justified even for self-defence under customary international law.^{*14} Self-defence as an exception must be interpreted restrictively. As both the International Law Commission^{*15} and the majority of the states participating in the Vienna Conference^{*16} stressed, the nature of the inviolability of the premises should be unqualified. Accordingly, they refrained from adding exceptions even for cases of emergencies; the possibility of appealing to self-defence should be treated with utmost caution. In any case, pretexts such as 'in the interest of national security' and 'there are serious suspicions' are certainly not enough to trigger applicability of the right of self-defence. When the incident at the Libyan People's Bureau was analysed later in the British parliament, it was noted that a few shots fired from a mission, even if they caused an injury or a death, would not warrant entry to the premises of the mission under self-defence.^{*17} This does not mean that self-defence is completely out of the question^{*18}; however, first it must be demonstrated that there is "a necessity of self-defence, instant, overwhelming, leaving no choice of means and no moment for deliberation".^{*19}

3.1.2. Duty to protect the premises of the mission

The duty to protect the premises of the mission imposes a positive obligation that has a much less clear content and allows differing interpretations. The performance of this duty may actually result in contradictions with fundamental rights and freedoms (for example, freedom of speech, assembly, and movement) laid down in constitutions and international agreements. There were no problems when the relevant provision of the Vienna Convention was drafted, as this duty had been firmly established in customary international law and was considered obvious.

A special duty means that the receiving state must do more for the protection of the premises of the mission than it would normally do to ensure public order. This duty is a positive obligation that requires active contribution from the receiving state. However, this is not an absolute duty, as "all appropriate steps" denotes that all measures taken must be proportional to the risk and dangers threatening the premises of the mission.^{*20} Therefore, it is unreasonable to assume that the receiving state shall assign a 24-hour large police unit to guard every diplomatic mission. However, if the receiving state is aware, for example, of potential dangers to the mission or hostile demonstrations to be organised near the mission or if the head of the mission informs the receiving state of, for instance, an act of trespassing or an attack in progress, then the receiving state is obliged to offer the mission protection that corresponds to the actual threats. For example, if a protestor is trying to enter the premises of the mission, throwing pamphlets there, damaging the building of the mission, or acting in any other hostile manner, he must be immediately made to cease and arrested if necessary.

^{*12} E. Denza. *Diplomatic Law: A Commentary on the Vienna Convention on Diplomatic Relations*. 2nd edition. Oxford University Press 2004, p. 124.

^{*13} R. Higgins. *The Abuse of Diplomatic Privileges and Immunities: Recent United Kingdom Experience*. – *American Journal of International Law* 1985 (79), pp. 643–644.

^{*14} See J. S. Beaumont. *Self-defence as a Justification for Disregarding Diplomatic Immunity*. – *Canadian Yearbook of International Law* 1991 (29), pp. 391–402 for a detailed discussion on the possibility to use self-defence.

^{*15} *Yearbook of the International Law Commission* (Note 10), pp. 55–56; *Yearbook of the International Law Commission*. Vol. I. New York: United Nations 1958, pp. 128–129.

^{*16} See E. L. Kerley. *Some Aspects of the Vienna Conference on Diplomatic Intercourse and Immunities*. – *American Journal of International Law* 1962 (56), pp. 102–104.

^{*17} J. S. Beaumont (Note 14), p. 394.

^{*18} The International Law Commission has referred to such a possibility. See *Yearbook of the International Law Commission* (Note 6), p. 97.

^{*19} *British Foreign and State Papers 1840–1841* (29), p. 1138.

^{*20} Lord Gore-Booth (ed.). *Satow's Guide to Diplomatic Practice*. 5th edition. London: Longman 1979, p. 111.

Some states have deemed it necessary to adopt special measures in order to prevent attack against and damage to the premises of the mission, as well as any disturbance of the peace of the mission and impairment of its dignity. For example, the United States Congress adopted a joint resolution (i.e., a resolution of the House of Representatives and the Senate together) that made it unlawful to display any flag, banner, placard, or other such devices meant to intimidate, coerce, or bring into public odium any foreign diplomat within 500 feet of a diplomatic mission within the District of Columbia.^{*21} Of course, such restrictions do not mean that organisation of political demonstrations is forbidden altogether. This would be very complicated — more likely impossible — to achieve in democratic states, as freedom of speech and assembly are fundamental freedoms or human rights guaranteed in national constitutions and international agreements. The receiving state simply has a duty to make sure that demonstrations do not get out of control and the privileges and immunities of diplomatic missions and their staff are not violated because of such demonstrations.

Beginning in 1982, regular demonstrations had taken place in front of the South African High Commission in London against the apartheid regime. Suddenly, in summer 1984, the police commander who was responsible for controlling the situation ordered all of the protestors to move away from the mission on the pretext that their activities disturbed the performance of official function by the mission and impaired its dignity. Everyone who refused to move was arrested. It is interesting to point out that never in the preceding two years had protestors been asked to move away from the mission or arrested for taking part in a demonstration. In addition, the police commander acted without consulting the Foreign and Commonwealth Office first.^{*22} A judge later ordered the arrested persons to be released and found that an appeal to impairment of dignity requires there having been abusive or insulting behaviour toward the mission, and that a peaceful political demonstration does not amount to such.^{*23} United States courts have frequently had a chance to examine whether the above-mentioned restrictions on demonstrations in the vicinity of diplomatic missions are constitutional. These debates were stopped (at least for now) by the Supreme Court with a somewhat controversial decision.^{*24} The Supreme Court confirmed the constitutionality of prohibition of congregation within 500 feet of a mission, provided that such gatherings are reasonably believed to threaten the security or peace of the mission. On the other hand, the prohibition to display a flag, banner, placard, or other such devices meant to intimidate, coerce, or bring into public odium any foreign diplomat was found to be unconstitutional, since it was a content-based restriction on political speech in a public forum and not an action narrowly tailored to serve a compelling state interest. Nevertheless, similar restrictions are provided, with slightly changed wording, in the United States Code^{*25}, making it a crime to intimidate, coerce, threaten, or harass a foreign official or to obstruct him in the performance of his duties^{*26} and to congregate within 100 feet of any diplomatic mission with an intention to threaten the peace and security of said mission.

After the Libyan People's Bureau incident, both the British parliament and the national government reviewed the rights and obligations deriving from the Vienna Convention. In its response to the report of the parliamentary Foreign Affairs Committee, the government stated that the duty to protect the premises of the mission is fulfilled if the functioning of the mission is not impaired, its staff do not feel threatened, and its staff and visitors are able to freely arrive at and leave the mission.^{*27} Too loud a noise may constitute a disturbance of peace. In Germany, harassment of a mission and its staff by means of noise, loudspeakers, or megaphones is not permissible. In addition, round-the-clock demonstrations impair the dignity of a mission.^{*28}

In the case of the Estonian embassy in Moscow, it was seen that the Russian authorities did not fulfil the obligations deriving from the Vienna Convention to protect the premises of the mission from intrusion or damage and to prevent disturbance of the peace of the mission or impairment of its dignity. Shortcomings were obvious, and they were pointed out by several states and organisations.^{*29} From 27 April to 5 May, the Estonian embassy

²¹ Joint Resolution to Protect Foreign Diplomatic and Consular Officers and the Building and Premises Occupied by Them in the District of Columbia, Public Resolution No. 79, 15.02.1938. See *American Journal of International Law* (Supp.) 1938 (32), pp. 100–101 for the text (it is actually more specific and broader in scope).

²² R. Higgins (Note 13), p. 651.

²³ *Regina v. Roques*, Bow Street Magistrates Court, June 1984.

²⁴ *Boos v. Barry*, 485 U.S. 312 (1988), United States Supreme Court, Judgment, 22.03.1988. See D. Thompson. *Boos v. Barry: Balancing Diplomatic Inviolability with the Freedom of Speech*. – *Temple International and Comparative Law Journal* 1989 (3), pp. 109–111 for a detailed analysis of the decision.

²⁵ 18 United States Code § 112 (b).

²⁶ The Supreme Court referred to this provision as a better phrased alternative. There remains the question the prohibition in the United States Code is really better in essence or is it actually a cosmetic difference, that is, the provision does not specifically touch upon the sensitive issue of the freedom of speech and the First Amendment.

²⁷ Cmnd 9497, Misc. No. 5 (1985), paragraph. 39.

²⁸ E. Denza (Note 12), p. 145.

²⁹ See, for example, "Tensions in Estonian-Russian Relations", United States State Department Press Statement, 2.05.2007, No. 2007/363. Available at www.state.gov/r/pa/prs/ps/2007/may/84181.htm (22.09.2007); "NATO statement on Estonia", NATO Press Release, 3.05.2007, No. (2007)044; A. Lobjakas. Euroopa Liit asus kaitsma Eesti diplomaate Moskvast (EU Started to Protect Estonian Diplomats in Moscow). – *Eesti Päevaleht Online*, 3.05.2007. Available at www.epl.ee/artikkel/384418 (22.09.2007) (in Estonian).

in Moscow was blockaded mainly by members of two Russian youth organisations — Nashi and Molodaya Rossiya. Because the mission is situated between two small streets, the round-the-clock demonstration was taking place on two sides of the mission. It was estimated that there were about 600 persons continuously present.^{*30} The protestors threw stones and paint at the mission, causing material damage and impairing its dignity.^{*31} Offensive and provoking slogans, such as ‘We reached Berlin; we will also reach Tallinn’, were painted on the walls of the mission.^{*32} At one point, the youth organisations threatened to demolish the mission and were sure that they could find legal justification for such an extreme action.^{*33} Such malicious activities do not constitute, in any manner, an acceptable demonstration near a diplomatic mission. Although the police kept people to a distance of a couple of metres from the mission and ordered a 3.5-metre-high wooden barrier to be erected on the one side of the mission and a barbed-wire fence to be built on the other, four activists succeeded in crossing these defences and tore down the Estonian flag from a flagpole on the premises of the mission.^{*34} These acts show clearly that the protection of the premises of the mission was inadequate and that the receiving state did not fulfil its obligations under the Vienna Convention. The situation did not improve, despite repeated requests by Estonia and promises by Russia that the security of the mission would be improved and conditions for normal performance of diplomatic and consular function would be guaranteed.^{*35} The receiving state has a separate obligation to fully facilitate the performance of official functions by the mission.^{*36} Although the latter is a very vague provision, it can be applied as an additional argument to support the request by the sending state. The functioning of the mission was disturbed in several respects, which means that the steps taken by the Russian authorities for guaranteeing protection were once again inadequate. Firstly, loud music playing around the clock from loudspeakers disturbed the functioning of the mission and impaired its dignity as discussed above.^{*37} Secondly, the protestors hindered entry to and leaving from the mission by both Estonian diplomats^{*38} and nationals^{*39} and also by other diplomats.^{*40} Estonian Foreign Minister Urmas Paet commented on the situation of the Estonian diplomats by saying that they were completely surrounded and were, in essence, being held hostage.^{*41} Because of the disturbance to the functioning of the mission, the consular section was closed.^{*42} Estonian nationals who were in Russia and in need of consular assistance were advised to contact the mission by telephone.^{*43} As mentioned above, the possibility of freely entering and leaving the premises of the mission is one important aspect of protection of the mission.

When commenting on the situation surrounding the Estonian embassy, the spokesman of the Russian Ministry of Foreign Affairs said that Russia had completely fulfilled all of its obligations under the Vienna Convention.^{*44} This is doubtful — and it is not correct even if one points merely to the fact that demonstrations are allowed in Moscow only in daytime. Even if the events taking place were lawful under domestic Russian law, this does not release Russia from a duty to follow the Vienna Convention as international law preventing a state from invoking its internal law as justification for its failure to comply with a treaty.^{*45} In explanation of events concerning the Estonian embassy, the Russian Ministry of Foreign took the position that Estonia was to be blamed for everything.^{*46}

³⁰ Noorteühendused on Moskva Eesti saatkonna blokeerinud (Youth Organisations Have Blocked Estonian Embassy in Moscow). – Postimees Online, 30.04.2007. Available at www.postimees.ee/300407/esileht/siseuudised/258003.php (22.09.2007) (in Estonian).

³¹ Foreign Minister strongly denounces the continued inactivity of the Russian authorities. Estonian Ministry of Foreign Affairs Press Release, 29.04.2007, No. 84-E.

³² Noorteühendused on Moskva Eesti saatkonna blokeerinud (Note 30).

³³ Vene noorteühendused ähvardavad lammutada Eesti saatkonna (Russian Youth Organisations Threaten to Dismantle Estonian Embassy). – Postimees Online, 29.04.2007. Available at www.postimees.ee/290407/esileht/valisuudised/257870.php (22.09.2007) (in Estonian).

³⁴ Estonian Flag Torn off Estonian Embassy in Moscow. Estonian Ministry of Foreign Affairs Press Release, 1.01.2007, No. 93-E.

³⁵ Noorteühendused on Moskva Eesti saatkonna blokeerinud (Note 30).

³⁶ Article 25 of the Vienna Convention.

³⁷ Noorteühendused on Moskva Eesti saatkonna blokeerinud (Note 30).

³⁸ Moskvast piirati Eesti suursaadiku autot (Estonia's Ambassador's Car Blocked in Moscow). – Eesti Päevaleht Online, 27.04.2007. Available at www.epl.ee/uudised/383735 (22.09.2007) (in Estonian).

³⁹ Foreign Minister strongly denounces the continued inactivity of the Russian authorities (Note 31).

⁴⁰ I. Taro. Saatkonna piirajad pääsesid lipu kallale (Besiegers of the Embassy Got Hold of the Flag). – Postimees, 2.05.2007 (in Estonian).

⁴¹ Statement by the Foreign Minister, Estonian Ministry of Foreign Affairs Press Release, 1.05.2007, No. 95-E.

⁴² M. Šmutov. Eesti saatkond Moskvast lõpetas konsulaartöö (Estonian Embassy in Moscow Discontinues Consular Work). – Postimees Online, 2.05.2007. Available at www.postimees.ee/020507/esileht/siseuudised/viimased_sundmused/258231.php (22.09.2007) (in Estonian).

⁴³ Noorteühendused on Moskva Eesti saatkonna blokeerinud (Note 30).

⁴⁴ Kamõnin: Venemaa ei ole diplomaatiliselt tava rikkunud (Kamynin: Russia not in Breach of Diplomatic Practices). – Eesti Päevaleht Online, 2.05.2007. Available at www.epl.ee/artikkel/384379 (22.09.2007) (in Estonian).

⁴⁵ Vienna Convention on the Law of Treaties, 23.05.1969, entered into force on 27.01.1980, 1155 UNTS 331, Article 27.

⁴⁶ Venemaa: Eesti saatkonna ümber toimuv on süüdi eestlased ise (Russia: Estonians Themselves at Fault for Situation around the Estonian Embassy). – Postimees Online, 2.05.2007. Available at www.postimees.ee/020507/esileht/valisuudised/258376.php (22.09.2007) (in Estonian).

3.2. Inviolability of the person

Personal inviolability is without doubt the cornerstone of diplomatic law, as even in ancient times people had to understand that reaching agreements and achieving mutual intercourse is difficult if envoys are killed when arriving or negotiating. By the time of the conclusion of the Vienna Convention, the principle of personal inviolability was so strongly established in customary international law that the commentary of the International Law Commissions on the respective article is clearly more than laconic if one takes into consideration its importance. At the same time, the commentary did include a very importance element; namely, it stated that the principle of personal inviolability does not exclude, in respect of the diplomatic agent, either measures of self-defence or, in exceptional circumstances, measures to prevent him from committing crimes or offences.^{*47} Personal inviolability has two important aspects: 1) a diplomat is not to be subjected to any form of arrest or detention, and 2) the receiving state must treat a diplomat with due respect and take all appropriate steps to prevent any attack on his person, freedom, or dignity.^{*48}

It may well happen that the police stop a diplomat in good faith, but as soon as it has been established that this person has diplomatic status, he must be released immediately. The diplomat may not be searched or, for example, forced to take a sobriety test. However, personal inviolability does not imply that the diplomat need not pass a security check, either manual or electronic, before boarding an aeroplane. If the diplomat refuses to submit to such a check, the airline company is not obliged to serve him. For example, the United Kingdom informed all diplomatic missions that airline companies have a complete right to check also diplomats in order to ensure the safety of persons on board. Diplomats were asked to co-operate fully with the security services of airlines.^{*49} According to the Vienna Convention, personal inviolability is unqualified: there are no explicitly mentioned exceptions, even for cases of emergencies. Certain limited exception may be derived from the right of self-defence and potentially also from the need to protect human lives. The possibility of the first exception has been confirmed by both the International Law Commission and the International Court of Justice, which stated that a diplomat caught in the act of committing an assault or other offence may, on occasion, be detained briefly by the police of the receiving state in order to prevent commission of the specific crime in question.^{*50} In 1947, the Moscow police were forced to, as a last resort, tie up a Brazilian diplomat in order to prevent him destroying the furniture in his hotel room. The Brazilian government did protest, but this was not justified in view of the circumstances.^{*51}

When discussing the protection of diplomats, the Vienna Convention does not explain the concepts 'all appropriate steps' and 'attack'. Unfortunately, these notions are not elaborated on, even in the later Convention on the Prevention and Punishment of Crimes against Internationally Protected Persons, Including Diplomatic Agents (1973).^{*52} What steps are appropriate depends, naturally, on the threatening dangers, and one has to take in account also reasonability and proportionality. In addition, the general conditions in the receiving state may be of noteworthy importance.^{*53} In Colombia, regarded as a very dangerous posting for diplomats, the government provides armed guards for all ambassadors and first secretaries and suggests special security advice.^{*54} Certain acts, such as murder, taking hostage, kidnapping, and threats, along with attempts to commit such acts, are clearly forbidden.^{*55} In German practice, round-the-clock demonstrations are considered to not only impair the dignity of the mission but also infringe personal inviolability.^{*56} The special duty to protect diplomats means that the receiving state must do more for the protection of the premises of the mission than it would normally do for ordinary people.

In the case of the Estonian embassy in Moscow, the most telling example of the violation of personal inviolability was an attack by a Nashi activist, during a press conference, against the person of the Estonian ambassador, Marina Kaljurand. According to the spokesman for the Estonian Ministry of Foreign Affairs, the ambassador was hit by a pepper-spray attack.^{*57} Then, when the ambassador was returning from the press conference, she was caught in an ambush. Two cars that had been waiting cut off the road so that the ambassador's car was not able to move forward and Nashi activists could surround her car, at the same time demanding that she leave

⁴⁷ Yearbook of the International Law Commission (Note 6), p. 97.

⁴⁸ Article 29 of the Vienna Convention.

⁴⁹ G. Marston. United Kingdom Materials on International Law. – British Yearbook of International Law 1986 (57), pp. 550–551.

⁵⁰ United States Diplomatic and Consular Staff in Teheran (Note 4), paragraph 86.

⁵¹ G. E. Silva. Diplomacy in International Law. Leiden: A. W. Sijthoff 1972, p. 93.

⁵² Convention on the Prevention and Punishment of Crimes against Internationally Protected Persons, including Diplomatic Agents, New York, 14.12.1973, entered into force on 20.02.1977, 1035 UNTS 167.

⁵³ See also Gore-Booth (Note 20), p. 122.

⁵⁴ E. Denza (Note 12), p. 216.

⁵⁵ See Article 2 of the Convention on the Prevention and Punishment of Crimes against Internationally Protected Persons, including Diplomatic Agents.

⁵⁶ E. Denza (Note 12), p. 145.

⁵⁷ Estonian Ambassador to Moscow was Attacked. Estonian Ministry of Foreign Affairs Press Release, 2.05.2007, No. 97-E.

the country. The special force OMON arrived five minutes later and dissolved the blockade and escorted the ambassador to the mission, freeing the road.^{*58} Also, the car of the Swedish ambassador was attacked when it was parked in front of the Estonian embassy; the flag and a mirror were torn off.^{*59} On a number of occasions, the duty to treat a diplomat with due respect and to prevent attacks on his person, freedom, or dignity was not fulfilled. For example, there were numerous dishonoured photos of the ambassadors and a banner suggesting that she should “return to [her] fascist country”.^{*60} Drawing a parallel with the protection of the premises of the mission, it may be said that the duty to protect diplomats is breached if they feel threatened. If one takes into consideration living and working under siege, continuous loud music and offensive chanting, attacks against the mission, and threats to demolish the mission, it may be easily concluded that necessary protection was not provided.

3.3. Freedom of movement

The ability to travel freely in the territory of the receiving state is very important for the performance of diplomatic functions. The protection of the interests of the nationals of the sending state is seriously hindered without such a freedom because diplomats cannot meet with their country's nationals. Protection of the interests of the sending state is equally hampered if diplomats are not able to meet with local authorities or diplomats from other missions. Lack of the freedom of movement affects also the ability of a diplomat to assess conditions and developments in the receiving state and to report thereon to the sending state.^{*61} In order to obtain a full and accurate picture of the prevailing conditions and ongoing developments in the receiving state, diplomats must have an opportunity to travel in different regions of the receiving state. If they are residing only in the capital, which usually is more developed than the rest of the receiving state, it is inevitable that the knowledge and understanding gained of the receiving state are incomplete.

Diplomats have not always been guaranteed freedom of movement. In Byzantium, the envoys sent to the emperor were met at the border and escorted to the capital via a specially prepared route. The purpose was to impress the foreigner with the powerfulness of Byzantium and to ensure that the envoy did not see things he was not meant to see. Moreover, the envoys were not allowed to freely choose a place of residence but had to live in a specially designed area where they were again impressed by various means of economic and military power of Byzantium. After the Second World War, the Soviet Union prohibited the members of diplomatic missions from travelling further than 50 kilometres from Moscow without a special permit. The latter were difficult to obtain, and diplomats who succeeded in receiving one remained under the constant surveillance of the police. Similar restrictions were imposed by Eastern European socialist countries and a little later by the People's Republic of China.^{*62} Such restrictions on the freedom of movement clearly were at odds with customary international law and were a subject of serious criticism from a variety of Western countries, some of which decided to impose the same restrictions in return. However, it was made known at the same time that these restrictions would be lifted as soon as the original restrictions were lifted.^{*63}

The Vienna Convention was expected to guarantee freedom of movement as clearly and broadly as possible. The issue was discussed by the International Law Commission, with the majority supporting the inclusion of a corresponding article in the convention (the most persistent objector was the Russian representative, Professor Grigory Tunkin^{*64}) but also wanting to make sure that the receiving state could restrict entry into certain areas for reasons of national security. Thus, the receiving state must ensure all members of a diplomatic mission freedom of movement and travel in its territory, except for those areas for which entry is prohibited or regulated for reasons of national security.^{*65} Certain restrictions are understandable because there are always areas that even local people are prohibited from entering, not to mention foreigners, on account of interests of national security. In addition, some areas may simply be dangerous, for example, because of riots or epidemics, so, as the receiving state has a duty to protect diplomats, they may be forbidden to travel to such areas.

However, making an exception to freedom of movement on grounds of national security is dangerous, as the latter is a very elastic notion that can cover very many and different situations if supported with skilful rhetoric. In any case, the creation of forbidden areas for different reasons may not render the freedom of movement

⁵⁸ Naši blokeeris Marina Kaljuranna auto (Nashi Blocked Marina Kaljuranna's Car). – Eesti Päevaleht Online, 2.05.2008. Available at www.epl.ee/artikkel/384271 (22.09.2007) (in Estonian).

⁵⁹ A. Lobjakas (Note 29).

⁶⁰ Moskvast piirati Eesti suursaadiku autot (Note 38).

⁶¹ Article 3 (1) (d) of the Vienna Convention.

⁶² *Revue générale de droit international publique* 1953 (57), p. 444.

⁶³ Gore-Booth (Note 20), p. 118.

⁶⁴ Yearbook of the International Law Commission (Note 10), pp. 85–86.

⁶⁵ Article 26 of the Vienna Convention.

illusory.^{*66} The Soviet Union's prohibition of travel further than 50 kilometres from the capital makes this freedom merely a beautiful declaration. The Soviet delegation informed other states at the Vienna Conference that Article 26 does not force the Soviet Union to give up its prevailing practice.^{*67}

In the case of the Estonian embassy in Moscow, the freedom of movement was repeatedly hindered for diplomats. This was discussed to some extent above, in connection with the inviolability of the premises of the mission. On the first day of the siege, the ambassador left the mission in order to give an interview to a television crew, but her car was blocked from moving, about 100 metres from the mission. The ambassador was locked in the crowd for half an hour before the OMON reached an agreement with the leader of Nashi and the car was reversed slowly back to the garage (this operation was accompanied by continuous scurrility).^{*68} Such behaviour directly prevented the ambassador from performing her official functions,^{*69} especially from representing and protecting the interests of the sending state by explaining to the public the situation back in Estonia. Hampering of the movement of the ambassador's car occurred several times. During the blockade, the diplomats of other missions were not able to enter the Estonian embassy.^{*70}

4. Russia's involvement in the events and its responsibility

The statements by the Russian authorities and other sources provide grounds to believe that Russia actually controlled what was happening around the Estonian embassy and fostered the continuation of the siege. Russia used the youth organisations for activities it did not want to carry out through agents of governmental authorities. It is public knowledge that the organisations behind the demonstrations have direct links with the Russian government and that the protestors were paid 550–1000 roubles per day for their presence around the Estonian embassy and participation in the demonstration.^{*71} Also, the law enforcement bodies allowed the protestors to decide who could enter or leave the mission. It was the latter who checked people's documents, while the police watched and admitted that Nashi were the ones with control over the situation.^{*72} The members of the Russian State Duma delegation that visited Estonia through the mediation of the European Union's Presidency declared that, if there were a political will, the police could clear the vicinity of the Estonian embassy in three minutes. However, the police had been given orders to provide only minimal protection.^{*73} The ability of the law enforcement organs to guarantee order at will was well demonstrated when the OMON quickly dissolved activists who tried to hamper the movement of a police car.^{*74} The police, among their other offences, did not react to the fact that the protestors ignored the rule that public gatherings and sanctioned demonstrations are allowed only during daytime in Moscow.

Taking into consideration the conduct of the protestors and the indifference or passive support of the law enforcement organs, a legitimate question arises about the responsibility of Russia for the events in the vicinity of the Estonian embassy. A state becomes responsible if the conduct 1) is attributable to that state under international law and 2) constitutes a breach of an international obligation of that state.^{*75} Traditionally a state is not held responsible for the conduct of private persons or their groups if they are not exercising elements of governmental authority.^{*76} Nevertheless, there are occasions on which the conduct of private persons or their groups is attributable to a state even if there exists no official link between them and that state. The level of responsibility depends on the kind of control the state has over these private actors.^{*77} The International Court of Justice found in the *Nicaragua* case that 'effective control' must be proved — that is, the state controlled or enforced the conduct in question.^{*78} This test imposes a quite unrealistic obligation on the other state to provide evidence of specific instructions or directions regarding specific conduct. The International Criminal

⁶⁶ Yearbook of the International Law Commission. Vol. II. New York: United Nations 1957, p. 137.

⁶⁷ E. Denza (Note 12), p. 170.

⁶⁸ Moskvas piirati Eesti suursaadiku autot (Note 38).

⁶⁹ See Article 3 of the Vienna Convention for traditional diplomatic functions.

⁷⁰ I. Taro (Note 40).

⁷¹ Statement by the Foreign Minister (Note 41).

⁷² I. Taro (Note 40).

⁷³ Statement by the Foreign Minister (Note 41).

⁷⁴ I. Taro (Note 40).

⁷⁵ Draft Articles on Responsibility of States for Internationally Wrongful Acts, UN Doc. A/56/10 (2001), Article 2 (hereinafter: the Draft Articles).

⁷⁶ R. Jennings, A. Watts (ed.). *Oppenheim's International Law*. Vol. I. 9th edition. Harlow: Longman 1996, pp. 502–503.

⁷⁷ See Article 8 of the Draft Articles.

⁷⁸ *Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States)*, Merits. – ICJ Reports 1984 (3), paragraph 115.

Tribunal for the former Yugoslavia has offered an alternative approach, in the *Tadić* case. Its Appeal Chamber believed that international law does not require that the control extend to the issuance of specific orders or instructions relating to specific acts and therefore it is enough if the state has 'overall control' over the private actors involved. Such control still demands more than mere financing or equipping of non-state actors and includes involvement in participation in or supervision of the planning.^{*79} The exact nature of the relationship between the Russian government and youth organisations Nashi and Molodaya Rossiya is not clear, but they have close links in that the Kremlin supports and finances their activities. Therefore, it is possible to speak of overall control by the Russian government over these organisations. It is potentially possible to hold Russia responsible for the conduct of the protestors because they were allowed to exercise certain elements of governmental authority; for example, as noted above, the protestors checked the documents of people moving in the area of the Estonian embassy and decided who was allowed to enter or leave.^{*80}

However, it is easier to hold a state responsible for its omissions. If a state has a duty to prevent certain private conduct or to refrain from supporting such conduct, the state becomes responsible for the inability to perform its duties. In this case, Russia had a duty to guarantee inviolability of the premises of the Estonian embassy as well as personal inviolability and freedom of movement for its staff. As Russia failed to secure these rights, it is responsible for its failure (indirect responsibility). This does not mean that Russia is also liable for the specific acts of the protestors (which would be direct responsibility). In November 1979, Iranian students captured the United States embassy in Teheran and took its staff hostage. The Iranian authorities neither prevented the students from doing so nor forced or persuaded them to leave the mission and release its staff.^{*81} The International Court of Justice found that Iran had completely failed to perform its duties with regard to protection of the mission and its staff (a case of indirect responsibility).^{*82} As Ayatollah Khomeini and other Iranian authorities later repeatedly and publicly approved the conduct of the students and referred to it as conduct of the Iranian nation, Iran acknowledged and adopted that conduct and became, as the situation continued, directly responsible for the acts of the students.^{*83}

5. Conclusions

According to long-established and universally recognised practice, receiving states must guarantee certain privileges and immunities to the diplomatic missions established in their territories and to diplomatic and non-diplomatic staff sent there. The purpose of these privileges and immunities is to guarantee to those person representing foreign government the maximum independence in the exercise of their official functions. Usually there is no need for such protection because states refrain from interfering, since they are interested in mutually friendly relations and wish for their own diplomatic missions and the staff thereof to have the widest possible freedom to operate in their receiving states. However, there are occasions on which the receiving state does not want to guarantee, partly or in full, these privileges and immunities, most likely as revenge or to assert pressure. One example of such behaviour is the siege of the Estonian embassy in Moscow, during which the mission was attacked (causing physical damage and impairing its dignity), the ambassador was assaulted (in both her person and her dignity) and her movement hindered outside the mission, and both the Estonian diplomats and nationals (as well as other diplomats) were prevented from freely entering and leaving the mission. These actions were carried out by several Russia youth organisations that were passively supported by the local authorities. Despite repeated reminders and requests, the law enforcement organs did little to protect the mission and its staff and to guarantee their rights. Russia maintained that it was convinced that it had done everything necessary and demanded under the Vienna Convention. An inescapable conclusion, therefore, is that the understanding of Russia of its obligations related to protection of a diplomatic mission and its staff is, at the least, weird and does not correspond to the spirit of the Vienna Convention or to relevant state and court practice. The conduct of Russia towards the Estonian embassy and its staff turned even the states that did not completely approve the moving of the Bronze Soldier against Russia. Such an attack on a diplomatic mission and its staff (especially in such a massive manner and for such a long time) is unprecedented in a civilised nation.

⁷⁹ *Prosecutor v. Duško Tadić*, Case No. IT-94-I-A, ICTY, Judgment of the Appeals Chamber, 15.07.1999, paragraph 145.

⁸⁰ Article 9 of the Draft Articles.

⁸¹ United States Diplomatic and Consular Staff in Teheran (Note 4), paragraph 66.

⁸² *Ibid.*, paragraph 68.

⁸³ *Ibid.*, paragraphs 69–74.



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Propaganda, Information War and the Estonian-Russian Treaty Relations: Some Aspects of International Law*

1. Introduction

Observation of the Estonian and international mass media reveals that propaganda issues became especially sensitive in the relations between Estonia and Russia in the first months of 2007, and tempestuous in April and May of the same year, when a memorial dating back to the Soviet occupation, known as the Bronze Soldier, was removed from Tõnismägi, Tallinn. The events came to be known as the Bronze Night after the ravages in Tallinn and East-Viru County over two nights, which occurred as a result of the (at that time still only planned) removal of the monument. Dmitry Rogozin, a former member of the Russian State *Duma*, who has served as an Ambassador of the Russian Federation to NATO since autumn 2007, declared to the news agency Rosbalt on 19 April 2007, i.e. before the displacement of the memorial, that Russia should use force: “I think that **desecration of the eternal peace of the tomb is a basis for war**. [...] An armed operation by a special unit would be a nice response to the provocative behaviour of fascists [author’s highlight — A.S.]”¹ Because of attacks on computer networks at that time, which the Estonian Ministry of Foreign Affairs considered a new chapter in the history of cyber conflicts, the Estonian press as well as statesmen and civil servants began to refer to the event as an **information war between Estonia and Russia** [author’s highlight — A.S.]² Is the claim that the propaganda became so exceptionally severe in 2008 true? In reality, wars of words have occurred quite often between our two countries. Instead, it is those moments when propaganda has not caught the attention of the public that should be considered exceptional. It turns out that historically, propaganda has affected the legal relations between Estonia and Russia. This article poses the question whether and to what extent the legal relations between Estonia and Russia have been affected by propaganda and whether this has had a wider effect on international law. In this article, I will examine the historical background of Estonian–Russian international legal relations in order to clarify the situation that had developed by 2007.

* This article represents the personal views of the author.

¹ Rogozin: Rossiyskiy spetsnaz dolzhen vyzvolit prakh voynov v Talline. – Informationsnoe agentstvo Rosbalt, 19.04.2007. Available at <http://www.rosbalt.ru/2007/04/19/293822.html> (27.04.2008).

² See. L. Anton, M. Pulliainen, et al. Cyber attacks hit Estonia. – Glance at the Mirror 2007. Estonian Ministry of Foreign Affairs, Tallinn 2008, p. 58. Available at http://web-static.vm.ee/static/failid/115/cyber_attacks.pdf (1.05.2008).

2. Clarification of Some Terms

Before turning to the actual research question and subject matter of the article, let us first clarify some basic concepts and notions. It must be emphasised that I will be discussing concepts that are often not regarded as primarily legal concepts — even if they have, as in the Estonian–Russian historical context, a legal dimension. Propaganda has a historical background in the relations between Estonia and Russia. Before explaining how, let us take a closer look at the notion itself. It is a historical fact that the **notion of propaganda** came to be used at the beginning of the 17th century, when in 1622 Pope Gregory XV founded an organisation, intended for Roman Catholic missionaries, called *Sacre Congregatio De Propaganda Fide*.^{*3} Philip M. Taylor, Professor of International Communication of the University of Leeds, has expressed the opinion that in Protestant societies, the word is still perceived as unpleasant because of its historical background.^{*4} Encyclopædia Britannica defines propaganda as follows: dissemination of information — facts, arguments, rumours, half-truths, or lies — to influence public opinion.^{*5} According to Soviet ideology, propaganda was meant for shaping a certain world view among the public, while so-called Western propaganda was meant to tie the public to the prevailing ideology, theory and information by the ruling class.^{*6} When looking at the ideology and acts of present-day Russia, we may say that some things have changed. The distinction between the so-called capitalist and Soviet propaganda has disappeared and the existing definition is a mix of both ideologies.^{*7}

Propaganda is perhaps the best-known notion, yet it is only one of the tools in communication between countries, which is aimed at imposing one's will on the other party to achieve political, military or social goals; such a set of measures may also be referred to as **subversive leverage**.^{*8} When it comes to furnishing the notion of propaganda (as part of psychological war) with content and its analysis in international law, subversive leverage is usually seen as a whole set. An information war is a considerably wider domain than simply propaganda.^{*9} Ingrid Detter Frankopan, Professor of International Law, has in her work defined four types of war and identified the subcategories of each type. This typology does not include information war.^{*10} When clarifying the legal problems at the core of this article, we cannot overlook the notions of Russian special services. In the USSR, subversive leverage was defined as **active measures**, i.e. operational activities of intelligence and counter-intelligence services, aimed at affecting the political activities of the target country, to take over initiative from the other party by using deception and undermining the enemy positions as well as by altering their plans in a manner that was necessary for achieving the foreign policy goals of the country taking measures of subversive leverage.^{*11} The article that describes the subversive leverage of Russia and the former Soviet Union contains a presentation made by the United States Information Agency (hereinafter: USIA) to the US House of Representatives in June 1992, which gives an overview of active measures. It is a Soviet term that refers to the use of manipulative techniques in the dissemination of information, including the selective use of slogans (a memorable political or commercial text that had military origins!^{*12}), disinformation and true information in substantiating their positions by persons who directly or indirectly wish to affect the positions and decision-making process of persons who have a decisive impact on the public of the country of location and thus also on the policy-making of the country.^{*13} The three main methods of subversive leverage are explained, which are called **white or grey or black**, respectively, according to the peculiarities of the tools and tactics used.^{*14} White or public measures are seen to include the information management of the public

³ L. J. Martin. *International Propaganda. Its Legal and Diplomatic Control*. Gloucester: Peter Smith 1969, p. 5.

⁴ P. M. Taylor. *Munitions of the Mind. A History of propaganda from the ancient world to the present era*. Manchester, New York: Manchester University Press 2006, p. 3.

⁵ See the definition of the term 'propaganda' in Britannica Online: Manipulation of information to influence public opinion. Available at <http://www.britannica.com/ebc/article-9375985> (27.04.2008).

⁶ *Sovetskiy Entsiklopeditseskiy Slovar'*. IV izdanie. Moskva 1989, p. 1080.

⁷ *Tolkovyy slovar' russkogo yazyka kontsa XX v. Sankt Peterburg*: Folio-Press 1998, p. 516.

⁸ Estonia has also used a long and ambiguous definition such as 'operation of active measures of foreign intelligence'. See Security Police of the Republic of Estonia. *Annual Review 2001, 2002*, pp. 18–20; Security Police of the Republic of Estonia. *Annual Review 2006*. Tallinn 2007, pp. 8–12 (the notion of information war has been used) pp. 32–36.

⁹ Ch. C. Joyner, C. Lotrionte. *Information Warfare as International Coercion: Elements of a Legal Framework*. – *European Journal of International Law* 2001 (12) 5, pp. 826–827.

¹⁰ I. Detter. *The Law of War*. Cambridge: Cambridge University Press 2000, pp. 38–58.

¹¹ *Kontrrazvedyvatelnyy slovar'*. Moskva 1972, pp. 161–162. See for comments and English translation: V. Mitrokhin. *KGB Lexicon. The Soviet intelligence Officer's Handbook*. London: Frank Cass 2002, p. 13 – intelligence methods, p. 251 – counter-intelligence methods.

¹² See the definition of the word 'slogan' at Dictionary.com: Slogan means a war cry or gathering cry, as formerly used among the Scottish clans. See <http://dictionary.reference.com/browse/slogan> (27.04.2008).

¹³ *Soviet Active Measures in the "Post-Cold War" Era 1988–1991. A Report Prepared at the Request of the United States House of Representatives Committee on Appropriations by June 1992 by the United States Information Agency, June 1992*. Available at http://intellit.muskingum.edu/russia_folder/pcw_era/exec_sum.htm (27.04.2008).

¹⁴ *Ibid.*, see chapters "Executive Summary" and "The Role of Active Measures in Soviet Foreign Policy". Available at http://intellit.muskingum.edu/russia_folder/pcw_era/exec_sum.htm (1.12.2008).

press and information services, both in their home country and through the information activities of embassies located abroad.^{*15} Grey or semi-public measures are seen as activities in which movement of information is administered through non-profit organisations and political parties, and subversive leverage.^{*16} Black or covert measures are regarded as undercover working of special service officials in news agencies.^{*17} It should also be noted that the USIA agency was established during the Cold War, in order to withstand Soviet Union propaganda.^{*18} In the United Kingdom and US, the notion of **covert action** is used instead of subversive leverage, but in a slightly narrower sense than in the case of the active measures of the former Soviet Union.^{*19}

3. Two Significant Treaties between Estonia and Russia

3.1. Peace Treaty of 1920

Clause 5 of Article VII of the Tartu Peace Treaty, entered into between the Republic of Estonia and the Russian Soviet Federative Socialist Republic on 2 February 1920, (hereinafter: Estonian–Russian Peace Treaty) provided: “Not to authorise the formation or presence in their territory of any organisation or groups whatsoever, which claim to govern the whole or part of the territory of the other Contracting Party, or the presence of representatives or officials of organisations and groups, whose object it is to overthrow the Government of the other party to the Treaty.”^{*20} This article prohibits the activities of organisations whose success inevitably and most directly depends on propaganda as it is impossible to achieve a change in state power without the involvement of a sufficient number of people. Furthermore in order to involve people, it is necessary to incite them to act. Propaganda is generally used to affect people to involve them in some sort of activity. L.J. Martin cited the Tartu Peace Treaty, entered into between Estonia and Russia in 1920, as an example of prohibition of propaganda in international law.^{*21} Below, I will examine some arguments presented by individuals participating in the conclusion of the Estonian–Russian Peace Treaty in 1920, as well as by their contemporaries, which indicates the importance of the role played by propaganda in signing the Treaty.

3.1.1. Arguments by the Russian party

A book on the Tartu Peace Treaty, published during the Soviet occupation, gave the following overview of the Russian positions for concluding the peace treaty: “At that stage of the negotiations, the Russian delegation mainly emphasised guarantees of actual security, which had to preclude the possibility that the Estonian territory could be used as a military platform against Soviet Russia, as it had happened in 1919. Already at the opening session of the conference, L. Karassin had emphasized: Without a certain guarantee that the peace will not transform simply into a military manoeuvre that is used to better prepare for a new bloodshed, we will not sign the treaty.”^{*22} The author of that monograph has worded the introduction to the chapter as “the principal position of the Soviet party” and noted that the draft Peace Treaty contained a clause that prohibited “the presence in the territory of any organisations or groups which claimed to govern the whole or part of the territory of Russia within the limits of Estonia as well as recruiting and mobilisation to the armies, organisations and groups of any other countries fighting against Soviet Russia.”^{*23} Clause 5 of Article VII

¹⁵ *Ibid.*, see chapter “‘White’ or overt active measures”. Available at http://intellit.muskingum.edu/russia_folder/pcw_era/sect_03.htm#White (1.12.2008).

¹⁶ *Ibid.*, see chapter “‘Gray’ active measures”. Available at http://intellit.muskingum.edu/russia_folder/pcw_era/sect_03.htm#Gray (1.12.2008).

¹⁷ *Ibid.*, see chapter “‘Black’ or covert active measures – see for details”. Available at http://intellit.muskingum.edu/russia_folder/pcw_era/sect_03.htm#Black (1.12.2008).

¹⁸ This day, these tasks are performed by the Bureau of International Information Programs. See their Web site <http://www.state.gov/r/iip/> (01.12.2008).

¹⁹ L. Scott. Secret Intelligence, Covert Action and Clandestine Diplomacy. – L.V. Scott, P. D. Jackson (eds.). Understanding Intelligence in the Twenty-First Century. Journeys in Shadows. London, New York: Routledge 2004, p. 163.

²⁰ Compiled by: L. Mälksoo. Rahvusvahelise õiguse lepingud (Treaties of International Law). Tallinn: Juura 2006, p. 598 (in Estonian). In 2005, a dispute developed about the Tartu Peace Treaty between historians and legal scholars (see E. Medijainen. Hidden Corners of the Tartu Peace. Available at <http://www.epl.ee/artikkel/284235> (1.12.2008) (in Estonian); H. Lindpere. Kas Tartu rahu kehtib? Mis tähendus on rahulepingul täna (Is the Tartu Peace Treaty Still Valid? What Meaning Has It Today?)? Available at <http://www.epl.ee/artikkel/284237> (1.12.2008) (in Estonian)) were of the opinion that the Tartu Peace Treaty did not apply, while L. Mälksoo adopted a different opinion. (See his article *Tartu rahuleping: kehtiv või kehtetu?* (Tartu Peace Treaty: valid or invalid). Available at <http://www.epl.ee/?artikkel=284590> (27.04.2008) (in Estonian)).

²¹ L. J. Martin (Note 3) p. 92.

²² E. Mattisen. Tartu rahu (Tartu Peace). Tallinn: Eesti Raamat 1989, p. 330 (in Estonian).

²³ *Ibid.*

of the Peace Treaty was set out in a similar wording.^{*24} When explaining the importance of the Tartu Peace Treaty, E. Mattisen mentioned the following: “The Tartu Peace Treaty marked the first breakthrough of the anti-Soviet intervention chain and blockade.” Here it was most important that Article VII of the Peace Treaty established mutual security guarantees. The existence of any forces, groups and organisations hostile to the other contracting party was prohibited on the territory of either of the countries. The military missions of the interventionists and the representatives of Russian White Guard “governments” had to leave Estonia after the conclusion of the Peace Treaty.^{*25} In a work created close to that by E. Mattisen on the arrow of time but with rapidly changing events, Professor of History Jüri Ant emphasises the importance of the Peace Treaty. The author’s position is especially fascinating regarding the provision that “[...] neither of the parties could maintain on its territory a corps or formations of forces hostile to the other party both in a military and ideological sense, had a visible effect.”^{*26} Ideology that was closely related to propaganda had been included in the Treaty for a reason. We may say that in that particular time and space, ideology was an integral part of the principal conditions of the Tartu Peace Treaty of 1920. Already a few months after the entry into the Peace Treaty, Estonia had to deal with both the recruitment stations of Russian refugees and propaganda which had been prohibited under the Treaty. The fact that problems related to the recruitment stations were serious is expressed by a note of the People’s Commissioner for Foreign Affairs of the Russian SFSR to Estonia, dated 10 July 1920.^{*27} The Russian monarchists residing in Estonia and the publications issued by the movements connected with them posed a problem for Estonia, since they criticised both Great Britain and Poland that were viewed as important allies at the same time.^{*28} Optants were also important for both parties, from the point of view of the ideological fight: Estonia screened them and Soviet Russia tried to send communists for party missions to Estonia among them.^{*29}

3.1.2. Estonia’s arguments

The work by Eduard Laaman ‘Birth of Estonia’s Independence’, published prior to Soviet occupation, noted the following: “Estonia has developed a draft peace and weapon suspension treaty, in which [...] Russia recognises Estonia’s independence, renounces propaganda in Estonia, makes reparations, compensates Estonian optants for nationalisation damage.”^{*30} According to E. Laaman, Russia required the following: “Estonia prohibits other armies except for the Estonian national army from staying in its territory [...]; bans organisations and groups or their representations, who claim to govern the Russian State or a part thereof; also prohibits recruiting to armies who aim at fighting Soviet Russia.”^{*31} The negotiations held to conclude the Peace Treaty also touched upon the issue of subversive leverage or among other things propaganda; the head of the Estonian delegation, Jaan Poska, explained to the head of the Russian party, Adolf Joffe, that Estonia had certain doubts concerning Soviet Russia’s intentions regarding the Treaty, illustrating this by the call of the Red Army “Further to Narva!” and the proclamation to punish Estonian white bandits. According to the author, “the declaration hit the tender spot of the enemy — propaganda”.^{*32} As soon as during the year following the conclusion of the Peace Treaty, the Minister of Foreign Affairs Ants Piip, who had participated in the signing of the Treaty, was compelled to send a note to the Russian Government because there were many problems With respecting the Treaty.^{*33} A. Piip pointed out the problems related to clause 5 of Article VII of the Peace Treaty, noting that at Fontanka 27, Petrograd, was located the Estonian department of the Russian Communist party, whose goal was to overthrow the Estonian Government.^{*34} A. Piip also mentioned that there was a political party school in Petrograd, assigned to send propagandists to Estonia.^{*35} Further, A. Piip draw attention to a provision of international law as regarded the detention of Estonian citizens in Russia, and stated that such action was a

²⁴ L. Mälksoo (Note 20), p. 598.

²⁵ E. Mattisen (Note 22), p. 412. Here it would be appropriate to stress the importance of the work in its time, expressed by a note on page 4 that the book was edited by Hendrik Allik (who contributed to the occupation of Estonia in 1940) and Karl Siilivask, PhD, who represented the Soviet paradigm in history.

²⁶ J. Ant. Eesti 1920. Iseseisvuse esimene rahuaasta (First Year of Peace during Independence). H. Arumäe (ed.). Tallinn: Olion 1990, p. 55 (in Estonian).

²⁷ *Ibid.*, p. 57.

²⁸ *Ibid.*, pp. 57–58.

²⁹ *Ibid.*, pp. 58–59.

³⁰ E. Laaman. Eesti iseseisvuse sünn (Birth of Estonian Independence). Stockholm: Kirjastus Vaba Eesti, Tryckeri AB Esto 1964, p. 671 (in Estonian).

³¹ *Ibid.*, p. 685.

³² *Ibid.*, pp. 696–697.

³³ A. Piip. Õiguse jõud (Power of Justice). Tartu: Ilmamaa 2007, pp. 203–213 (in Estonian).

³⁴ Considering the size of Petrograd, Fontanka 27 was not very far from the headquarters of Okhranka, the Secret Police of the Russian Empire, located at Fontanka 16, the experience and staff of which were later used by Bolshevik Russia. For details, see Ch. A. Ruud, S. A. Stepanov. Fontanka 16. The Tsars’ Secret Police. McGill-Queen’s University Press 1999.

³⁵ A. Piip (Note 33) p. 210.

direct violation of the most important principles of the Peace Treaty, founded on the assumption that the parties did not interfere in each other's internal matters and renounced mutual propaganda, while also noting that Estonia strictly fulfilled the condition.³⁶ An article by A. Piip in 1922, once again, stressed the importance of propaganda: "And were we not threatened by the possible Bolshevik propaganda all the time? We have peacefully digested it, thanks to the sanity of our people. We have set ourselves free from the slavery of words and the miracles of Bolshevik declarations."³⁷ The number of all the passages mentioning propaganda in the articles by A. Piip suggests that the phenomenon was critical before the Second World War. In his paper written in 1930, the tenth anniversary of the Treaty, A. Piip observes regarding Article VII, which sets out the military guarantees, separately referring to the dissolution of the Yudenich Army and the Estonian Red Division, "However, the performance of the provisions of clause 5 of that Article by Russia leaves much to be desired, as the Estonian section of the Comintern, regardless of the prohibition under the Treaty, continues to arrange for the "Red Estonian Government", the saddest act of which was the organisation of a rebellion in Estonia on 1 December 1924". After that, the author proceeded to note that the issue (i.e. discontinuation of agitation) had shown improvement.³⁸ In hindsight, we know that the apparent improvement of relationships, as it had seemed to A. Piip, was only illusory, and the author of the above quote had to experience the consequences imposed on Estonia by the outbreak of World War II in a GULAG. The Tartu Peace Treaty was the corner stone of the relations between Republic of Estonia and Soviet Russia (or later: the USSR), although after the restoration of Estonia's independence in 1991, Russia no longer recognizes this Treaty. An interesting interpretation of the consequences stemming from legal succession for Estonia has been presented by the former official of the Russian ministry of Foreign Affairs Mikhail Demurin who opined to the news agency Regnum in 2006, that Estonia should be declared an enemy and subjected to enforcement action under Article 107 of the UN Charter (ref. to Article 53), because by demanding recognition of the continuity with the pre-World War II Republic of Estonia positioned itself as an ally to Nazi Germany, with all the ensuing consequences.³⁹ It remains unclear, however, how Estonia's State identity with the pre-World War II republic would imply that Estonia as a State would have fought on the Axis side. The USSR had illegally occupied and annexed Estonia and the other two Baltic States already before Germany attacked the USSR in 1941.

3.2. Treaty on foundations of Estonian–Russian relations of January 1991

In January 1991, another treaty between Estonia and Russia was concluded. The status of the treaty partners was, however, peculiar. The independence of the Republic of Estonia was only restored in August 1991 and in January 1991, the Russian Federation (then part of the USSR), was not internationally recognised as a sovereign State either. However, what is fascinating and noteworthy in the present context, is that Article VIII of the January 1991 Treaty is very similar to the 1920 Tartu Peace Treaty provision, referred to: "The High States Parties undertake, on their territories to prohibit by their legislation the creation of such organisations and groups, the aim of which is the violent destruction of the independence and sovereignty of the other party or a violent surge to power, and impede their activities". The Article contained a provision characteristic of the present era that had not been there earlier and that governed cooperation against organised and international crime. Hence, the impact of the Estonian–Russian Peace Treaty of 1920 was rather important in shaping the new Treaty.

3.3. Questions raised

The similar provisions of the two Treaties prohibit propaganda, which is rather significant considering the actual political relations between our countries. Some questions can be raised based on the provisions of the above Treaties: whether it is the peculiarity of the two bilateral treaties or that the provisions were frequently used in international law at the time, and what was the historical background of such provisions? Does the UN Charter contain a regulation similar to the Peace Treaty between Estonia and Russia? The peace treaties of two of Estonia's close neighbours, Finland and Latvia, do not give a uniform clarification whether it is a peculiarity of a specific bilateral treaty or a provision frequently used in international law. Unlike the Estonian–Russian Peace Treaty, the Russian–Finnish Peace Treaty, concluded in Tartu on 14 October 1920, does not contain provisions prohibiting propaganda. Yet the Treaty set out in detail the provisions related to

³⁶ *Ibid.*, p. 212.

³⁷ *Ibid.*, pp. 272–273.

³⁸ *Ibid.*, p. 240.

³⁹ M. Demurin. *Estoniya mozhet byt' priznana "vrazheskim gosudarstvom"* po ustavu OON. – *Informatsionnoe agentstvo Regnum*, 10.12.2006. Available at <http://www.regnum.ru/news/752818.html> (1.05.2008).

the demilitarisation of the Gulf of Finland.^{*40} The Latvian–Russian Peace Treaty, signed in Riga on 11 August 1920, again contains provisions that are rather similar to those indicated above when discussing the Estonian–Russian Peace Treaty. Hence, clauses 1 and 2 of Article IV of the Treaty are relatively similar to clause 5 of Article VII of the Estonian–Russian Peace Treaty.^{*41} It must be only added that the same Article also contains supplementary clauses arising from the peculiarities of Latvia, related to the activities of the Latvian Red Riflemen. The Lithuanian–Russian Peace Treaty, signed on 12 July 1920, contains clause 1 of Article IV that essentially has the same wording as the above-mentioned Article in the Estonian–Russian Peace Treaty.^{*42} Russia and Soviet Ukraine on the one part and Poland on the other part concluded on 12 October 1920 a treaty in order to start peace negotiations: Article II of the Treaty provides that the parties refrain from intervention in each other's affairs and undertake not to create or support the activities of groups that aim at overthrowing the governments or state power of the parties to the Treaty.^{*43} On 18 March 1921, the same countries signed a Peace Treaty that contained a more detailed regulation compared to the Treaties mentioned above. The declaration of Article V promised to fully respect national sovereignty; in addition, intervention in internal matters, agitation, propaganda and any intervention was prohibited along with support for such activities, such as activities of various groups, the aim of which was the overthrowing of the government or state power of the other party, and the presence of the members of such groups on the territory of the parties and recruitment for such groups, serving as the most detailed Treaty of that kind, to which Russia was a party.^{*44} Article V of the Russian–Persian Treaty, entered into on 26 February 1921, sets out that the parties undertake not to allow the activities of armed groups, the aim of which is battling against the other party, and prohibit provision of support to such movements for transit operations; however, compared to the above Treaties, there were no references to ideological fighting or the overthrowing of the state.^{*45} Article VIII of the Russian–Turkish Treaty of 16 March 1921 reminds one of the Estonian–Russian Peace Treaty, but with the important addition that Russia and Turkey undertook a mutual obligation to ensure in the Caucasian Soviet Republics regulation of the activities of such groups that aimed at overthrowing the present government.^{*46} Thus, when answering the question raised above, it may be said on the basis of peace treaties into which Russia entered in 1920 and 1921 **that the provisions prohibiting propaganda, included in the Estonian–Russian Peace Treaty, were not exceptional, but shaped the development of international law in this field.** Several treaties to which Russia was a party revealed the peculiarities of the other states parties; for example, analysis of the Finnish and Latvian treaties shows that they lacked the provisions included in the Estonian–Russian Peace Treaty or the provisions had been supplemented to a lesser degree. The modern principle of non-interference was established in international law at the time of the Congress of Vienna (1815), when it was set forth that the parties had to respect mutual public order and it was promised to preclude revolutionary excesses.^{*47} Prevention of revolutionary excesses was not thinkable without precluding propaganda. It appears that the above-described Russian treaties proceed from the same principle. Further to the present day, we should begin with the world order after World War II, in which the United Nations and the UN Charter had to play a decisive role in international law.^{*48} However, it soon became clear that the expectations regarding the new world order did not come true and the former allies became enemies for several decades, in the period known as the Cold War. The world that was split up mainly into two ideologically opposed parts during the Cold War served as a testing laboratory for the implementation of various methods, including subversive leverage. Although the post-Cold War world lived in a sort of euphoria at the beginning of the 1990s, which was true also according to experts in international law, who expected a certain renaissance of international law, 11 September 2001 considerably altered the great expectations for international law, the International actors became more sober.^{*49}

⁴⁰ Dokumenty vneshney politiki SSSR. Moskva: Gosudarstvennoe izdatel'stvo politicheskoy literatury 1959, pp. 265–280. See, e.g., Article 13 the Russian–Finnish Peace Treaty prohibited certain activities of military nature on Stora Tyterskär / Suuri Tytärsaari in the Gulf of Finland. The Russian–Finnish Peace Treaty generally contained more provisions governing claims for damages between the two countries and issues related to shipping (including issues concerning warships).

⁴¹ *Ibid.*, the Latvian–Russian Peace Treaty, pp. 103–104.

⁴² *Ibid.*, the Lithuanian–Russian Peace Treaty, pp. 31–32.

⁴³ *Ibid.*, the Treaty in order to start peace negotiations between Russia and the Soviet Ukraine on the one part and Poland on the other part, p. 248.

⁴⁴ *Ibid.*, the Peace Treaty between Russia and Soviet Ukraine on the one part and Poland on the other part, pp. 623–624.

⁴⁵ *Ibid.*, the Russian–Persian Treaty, p. 538.

⁴⁶ *Ibid.*, the Russian–Turkish Treaty, p. 600.

⁴⁷ For details, see S. C. Neff. *War and the Law of Nations: A General History*. Cambridge University Press 2005, pp. 219–221.

⁴⁸ L. Mälksoo (Note 20), pp. 23–41.

⁴⁹ See M. Koskeniemi. *From Apology to Utopia*. Cambridge University Press 2007, p. 563.

4. Events of April 2007 and their impact on international law

As mentioned in the introduction to this paper, many people believed that tension in the relations between Estonia and Russia increased at the beginning of 2007. Each story has a prologue. The events related to the entry into the boundary agreement between the Republic of Estonia and Russian Federation in Moscow on 18 May 2005 can be brought as an example of complicated legal relations. On 20 June 2005, the Estonian *Riigikogu* supplemented the agreement with a Ratification Act^{*50}, setting out that the agreement partly alters, in accordance with the Constitution, the line of the state border defined in the Tartu Peace Treaty, entered into between Estonia and Russia on 2 February 1920, but does not affect the rest of the Tartu Peace Treaty nor does it pre-determine the handling of the bilateral issues not related to the boundary agreements. The adoption of the Ratification Act triggered somewhat unexpected consequences: on 22 June 2005 (at the anniversary of the start of World War II in the Soviet Union), Russia announced that because of the “territorial claims made by Estonia” the agreement cannot be ratified in the State *Duma*, and withdrew its signature from the agreement. When returning to the more tense relations in 2007, one of the reasons behind them was once again international law. The Estonian *Riigikogu* adopted the Military Graves Protection Act^{*51} that relied on Article 34 of the Protocol Additional to the Geneva Conventions of 1949, and relating to the Protection of Victims of International Armed Conflicts (Protocol 1). Based on § 8 (2) of the Act, in April of the same year, the Government of the Republic of Estonia decided to relocate the Bronze Soldier memorial because of the unsuitable site of the grave and the divisive public interest that did not ensure peace for the grave.^{*52} The Russian-speaking minority residing in Estonia was influenced by the TV channels owned by the Russian State and viewable across the border, in the programmes of which it was alleged that the Estonian Government was attempting to destroy the memorial and thereby desecrate the memory of the Russian soldiers fighting Nazism. Estonia was also blamed for re-writing the history of World War II. “We are witnesses to the information war against Estonia which already reminds of an **ideological aggression** [author’s highlight. — A.S.],” said the President of Estonia.^{*53} It is interesting to note that the UN had held an intense dialogue about the notion of ideological aggression in the 1950s, the components of which included propaganda of national hatred, Nazism and fascism.^{*54} The Bronze Soldier memorial was erected to the soldiers of the Soviet Union who presumably died in conquering Tallinn in 1944. It is a historical fact that when withdrawing from Tallinn on 22 September 1944, the German Army did not engage in any battles with the Red Army heading for the city.^{*55} Instead, the advancing Russian units encountered the Estonian flag flying in the tower of Tall Hermann, a symbol of State power in Tallinn, there were no casualties.

Attacks against the computer networks of the Estonian State and companies in May 2007 were widely discussed all over the world; articles were published in the US, British, French as well as German magazines, military journals and computer journals.^{*56} How could such relations be seen from the point of view of international law, whether international law was violated and whether the development of technology has changed the relation between international law and propaganda that may transfer to attacks against computer systems? It is a widely known fact that Article 2 of the UN Charter prohibits the threat of force against the territorial integrity, political independence or in any other manner inconsistent with the purposes of the United Nations. The preamble declares tolerance and expresses the desire to live in peace as good neighbours. Articles 19–20 of the UN International Covenant on Civil and Political Rights define the freedom of opinion to impart information and ideas of all kinds, regardless of frontiers and stresses the responsibility accompanying dissemination of information as well as prohibits propaganda for war and any advocacy of national, racial or religious hatred.^{*57} Article 3 (b) of UN resolution 3314 sets out the legal definition of aggression, defining it as the bombardment of a state by any weapons.^{*58} It is highly doubtful if the interpretation of the provision would include information weapons. At present, doubts have been voiced repeatedly if the UN Charter can be implemented, also in relation to subversive leverage; it has been mentioned that the Charter may serve as an aid but it would be

⁵⁰ Eesti Vabariigi ja Vene Föderatsiooni vaheline Eesti-Vene riigipiiri leping. – RT II 2005, 18, 59 (in Estonian).

⁵¹ Sõjahaudade kaitse seadus. – RT I 2007, 4, 21 (in Estonian).

⁵² Press Release of the Estonian Ministry of Foreign Affairs about the relocation of the monument, 27.04.2007. Available at http://www.vm.ee/eng/kat_138/8370.html?arhiiv_kuup=kuup_2007 (1.05.2008).

⁵³ See statement made by the President of Estonia Toomas Hendrik Ilves, 30.04.2007. – 16 kevadpäeva (Sixteen Days in Spring). Politseiamet, May 2007, p. 16 (in Estonian).

⁵⁴ B. S. Murty. The International Law of Propaganda. The Ideological Instrument and World Public Order. New Haven: New Haven Press 1985, pp. 160–167.

⁵⁵ Estonia 1940–1945. Reports of the Estonian International Commission for the Investigation of Crimes Against Humanity. Tallinn: Estonian International Commission for the Investigation of Crimes Against Humanity 2006, p. 1080.

⁵⁶ Glance at the Mirror (Note 2), pp. 58–7. Available at <http://www.un-documents.net/a29r3314.htm> (1.05.2008).

⁵⁷ Kodaniku- ja poliitiliste õiguste rahvusvaheline pakt. – RT II 1993, 10–11, 11 (in Estonian).

⁵⁸ United Nations A/RES/29/3314 (XXIX). Definition of Aggression. Available at <http://www.un-documents.net/a29r3314.htm> (1.05.2008).

of no use in achieving certain goals in cyberspace, where it is very difficult to locate enemy stations as well as organise defence.^{*59} On 1 November 2007, the UN Disarmament and International Security Committee adopted a resolution that concerns developments in the field of information and telecommunications in the context of international security. The resolution was initiated by Estonia along with the other EU Member States, who called on all UN Member States to accede to the Council of Europe Convention on Cybercrime of 2001.^{*60} Portugal, holding the Presidency of the European Union, made a statement after the adoption of the resolution, in which it highlighted potential threats to cyber security, which could originate from organised criminals, terrorists or coordinated attacks by individuals influenced, for example, by **political propaganda**.^{*61} What is the opinion of Estonia's neighbour to the east? A representative of the free press in Russia, *Novaya Gazeta*, that also quoted the Estonian views, published an article in May 2007, in which the Estonian Minister of Defence said that the cyber attacks on the state servers served as military aggression and some attacks originated from Russian national institutions.^{*62} Although in 2007, Russia denied any connection to cyber attacks against Estonia, things have slightly changed by 2008. The Head of the Centre of Military Forecasting, Anatoly Tsyganok opined in the newspaper *Gazeta* that cyber attacks against Estonia did not violate international law because there existed no such provisions that could be violated. The Colonel considered the attacks successful and noted that NATO had nothing to beat Russia in this regard, thus indirectly admitting to Russia's participation in the attacks against Estonia.^{*63} It was probably these principles that served as the basis for the doctrine, according to which it was not reasonable to attack the other country using conventional means since it was more useful to attack the enemy's knowledge pool using means of the information war.^{*64} The Martens Clause, formulated at the Hague Peace Conference of 1899 by the famous Russian international law expert of the Estonian descent, Friedrich Fromhold Martens (1845–1909), stipulates that: "populations and belligerents remain under the protection and empire of the principles of international law, as they result from the usages established between civilized nations, from the laws of humanity and the requirements of the public conscience".^{*65} Already in 1948, the US Military Tribunal used the Martens clause in the so-called Krupp case, noting that the clause went beyond being a mere declaration in the Hague convention, which should also be applied if necessary when new circumstances that had not surfaced before appeared in military activity.^{*66} It would also be appropriate to mention Protocol Additional to the Geneva Conventions of 12 August 1949, relating to defence in armed conflicts, Article 36 of which (new weapons) stated that "**in the study, development, acquisition or adoption of a new weapon, means or method of warfare** [author's highlight – A.S.], a High Contracting Party is under an obligation to determine whether its employment would, in some or all circumstances, be prohibited by this Protocol or by any other rule of international law applicable to the High Contracting Party".^{*67} Such a provision of international law should not be unfamiliar to a military expert of a civilised country. Military experts certainly would know about these kinds of existing norms. I. Detter Frankopan also placed information war in the chapter on armament limitations and noted that although the problem had been acknowledged on the international level, there were few studies, but in principle it could be agreed that it was, in a sense, a new type of warfare.^{*68} The US scholar L. John Martin, who studied the legal and diplomatic regulation of propaganda in the 1950s and 1960s, arrived at a conclusion that there were few possibilities on the international level to control propaganda or regulate it, with a sole exception being war propaganda that was prohibited.^{*69} The work was published long ago; has anything changed significantly since then? The most important changes have certainly been the introduction of cross-border television and, above all, the Internet, which does not essentially impose any restrictions on dissemination of information and hence also propaganda. If someone disseminates war propaganda, how can the individual be held liable if the act is committed in one country, but information is disseminated via a server located in a third country? The legal scholars analysing jurisdiction on the Internet have concluded that on the Internet, we could not speak about territoriality but the 'right of a server' that bears resemblance to the Geneva Convention on the

⁵⁹ Ch. C. Joyner, C. Lotrionte (Note 9), p. 827.

⁶⁰ See Convention of Cybercrime. – RT II 2003, 9, 32.

⁶¹ Press release of the Estonian Foreign Ministry. UN Approves Resolution Related to Cyber Attacks, 2.11.2007. Available at http://www.vm.ee/eng/kat_138/8979.html?arhiiv_kuup=kuup_2007 (1.05.2008).

⁶² A. Soldatov. Kiber-syurpriz. – *Novaya Gazeta*, Nr. 40, 31.05.2007. Available at <http://www.novayagazeta.ru/data/2007/40/18.html> (27.04.2008).

⁶³ A. Novikova, V. Lyubartas. Voенно-virtualnyy alyans. – *Gazeta*, Nr 23, 8.02.2008. Available at <http://gzt.ru/world/2008/02/07/220025.html> (27.04.2008).

⁶⁴ S. P. Kanuck. Information Warfare: New Challenges for Public International Law. – *Harvard International Law Journal*, Winter 1996, p. 290.

⁶⁵ See Martens' Society's Biographical Note — Friedrich Fromhold Martens. Available at the homepage of the Martens Society at <http://www.martens.ee/?id=10456> (1.05.2008).

⁶⁶ D. Fleck. Friedrich von Martens: A Great International Lawyer from Pärnu. – *Baltic Defence Review* 2003 (10) 2, p. 23.

⁶⁷ Available at <http://www.unhcr.ch/html/menu3/b/93.htm> (3.12.2008).

⁶⁸ I. Detter (Note 10), pp. 272–273.

⁶⁹ L. J. Martin (Note 4).

High Seas and the Outer Space Treaty.^{*70} Referring to the Geneva and Hague conventions, the Russian scholar A. Feodorov opines that the use of information war methods should be equated with the use of weapons of mass destruction although it would be problematic.^{*71} In 2006, D. Brown suggested that the use of information systems in armed conflicts be regulated by an international convention.^{*72} As a result of the events in Estonia in 2007, D.B. Hollis made a proposal to regulate by international law information operations that would cover both propaganda and cyber attacks.^{*73} Thus, it is planned to regulate the no man's land on the Internet, which inevitably involves limitations on subversive leverage and propaganda. But is it possible to hold countries liable for propaganda and cyber attacks? Although it is disputable at the moment, the Articles on Responsibility of States, approved at the UN General Assembly in 2001 (not in force yet), prove helpful, in which Article 8 states that "the conduct of a person or group of persons shall be considered as an act of the state under international law if it is established that such person or group of persons was in fact acting on the instruction of, or under the direction or control of that state in carrying out the conduct."^{*74}

5. Conclusions

Subversive leverage has a historical background in the relationships between Estonia and Russia, in a political as well as in international and legal context. The events occurring in 2007 have paradoxically contributed to the development of international law in cyberspace, which gives reason to hope that cyber attacks on computer networks will be regulated in international law on the UN level in the coming years; the efficiency of such regulation is another question. There is both practical need as well as the interest on the part of the European Union Member States and the USA to regulate issues regarding cyber terrorism on an international level. Production of new international law in this field is an inevitable part of the global civilisation process. The civilisation process usually involves reduction in human desires.^{*75} The hope that can be felt in international law for the legal regulation of cyberspace cannot be seen in the regulation of subversive leverage at an international level, above all, because of a lack of interest by countries, notwithstanding the efforts made by our neighbour to the east.^{*76} There is no good without bad and the same applies to the legal relations between Estonia and Russia that probably had a significant effect on the further development of international law in the fields described above. The paper showed that, in a historical context, Estonian–Russian bilateral relations have already had a more general effect on international law.

⁷⁰ D. C. Menthe. Jurisdiction in Cyberspace: A Theory of International Spaces. – Michigan Telecommunications and Technology Law Review 1998 (4), pp. 93–97.

⁷¹ A. Feodorov. Informatsionnyy bezopasnost' v mirovom politicheskom protsesse. Moskva: MGIMO 2006, pp. 103–110.

⁷² D. B. Hollis. Why States Need an International Law for Information Operations. – Lewis & Clark Law Review, winter 2007, pp. 1023–1061. Available at http://www.lclark.edu/org/lclr/objects/LCB_11_4_Art7_Hollis.pdf (1.05.2008).

⁷³ United Nations A/RES/56/83. Responsibility of States for internationally wrongful acts. Available at <http://daccessdds.un.org/doc/UNDOC/GEN/N01/477/97/PDF/N0147797.pdf?OpenElement> (1.05.2008).

⁷⁴ D. Brown. A Proposal for and International Convention to Regulate the Use of Information Systems in Armed Conflict. – Harvard International Law Journal, winter 2006 (47) 1, pp. 179–221.

⁷⁵ The Civilizing Process. Vol. II: State Formation and Civilization. Oxford: Blackwell 1982. See, e.g., N. Elias. The Civilizing Process. The Civilizing Process. Vol. II: State Formation and Civilization. Oxford: Blackwell 1982.

⁷⁶ D. B. Hollis (Note 72), p. 1037; A. Feodorov (Note 71), pp. 187–204.



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Specificatio in Baltic Private Law and Production (*Verarbeitung*) in the Baltic Private Law Act — Continuity or Change?

In the second half of the 19th century, the private law of the Baltic Sea provinces^{*1}, which were a part of the Russian Empire, took an important turn — in 1864, the codification of Baltic private law^{*2} entered into force in the Baltic Private Law Act (BES). Until then, different laws applied for the Baltic Sea provinces, which included in addition to medieval bylaws also chivalric and regional laws and the norms of Swedish, Russian, and Polish laws, with subsidiary application of Roman laws, and which generally can be called Baltic provincial law. Roman Law was recepted into the system to a greater extent from the 13th century. In 18th–19th-century court practice, Roman Law was allegedly preferred to the local law even if local laws should have been applied as primary sources; a contemporary work^{*3} states (in translation): “Roman Law — to that extent it is glossed — is recepted in its entirety in Germany and also in Livonia and Estonia and is used everywhere where the norms of Roman Law did not derive from the special Roman government or where the principles of Roman Law are not in direct opposition to the principles of the provincial law”.^{*4}

Unlike the laws adopted in Western Europe in the 19th century generally, the purpose of the BES was not to create a new, modern private law by means of a legislative reform. On the contrary, the general ideology of the

¹ The Baltic provinces included Estonia (Estland), Livonia (Livland), and Curonia (Kurland). The province of Estonia consisted of the northern half of present-day Estonia. Livonia comprised the territories of present-day South Estonia and North Latvia. Curonia comprised the western and southern parts of Latvia.

² *Provincialrecht der Ostseegouvernements. Dritter Theil. Privatrecht. Liv-, Est- und Curländisches Privatrecht. Zusammengestellt auf Befehl des Herrn und Kaisers Alexander II.* St. Petersburg: Buchdruckerei der Zweiten Abtheilung Seiner Kaiserlichen Majestät Eigener Kanzlei 1864.

³ G. v. Bunge. *Wie kann der Rechtszustand Liv, Esth- und Curlands am zweckmässigsten gestaltet werden?* Riga, Dorpat: Lang 1833, p. 32.

⁴ F. G. v. Bunge. *Das liv- und esthländische Privatrecht. 2. Ausgabe. I Theil.* Reval: Kluge Verlag 1847, p. 31. The most comprehensive books on Roman Law in the Baltic Sea provinces are by Hermann Blaese. See H. Blaese. *Einflüsse des römischen Rechts in den Baltischen Staaten.* IRMAE 1962; H. Blaese. *Bedeutung und Geltung des römischen Privatrechts in den baltischen Gebieten.* Leipzig: Verlag von T. Weicher 1936.

Russian Empire's codification movement and the intention of Friedrich Georg von Bunge^{*5} was to compile^{*6} existing private law and create *nova structura veterum legum*.^{*7} Bunge claimed in his programmatic essay on the scientific treatment of Baltic private law and its handling in codification that, in drafting of the future law, the principles of Roman Law should be avoided as much as possible.^{*8} At the same time, he admitted that Roman Law is a common element of all provincial laws and excluding Roman Law from provincial law would mean an incomplete treatment of the local private law. This treatment of local laws had to be "trustworthy and complete".^{*9} Therefore, the future code had to be a complete compilation of all laws that were to be in force in the various provinces, including Roman Law, where it was in force in a subsidiary role as *ius commune*.

In 1833, Bunge commented also on the earlier private law codification draft of 1831, which was in force in the Baltic provinces at the time. He criticised the fact that "single provisions do not derive from the sources of law in force in the Baltic Sea provinces but are copied word for word from the General National Law for the Prussian States, as has become evident after a closer investigation".^{*10}

The aim of the present article is to analyse the birth of the norms of an institute in the Baltic provinces that ran counter to general modernisation in the 19th century, using one specific legal institution, specification, as an example. This is the institution whose importance was the greatest in pre-industrial society and in cases of production by artisans. The field of use of specification has decreased in modern society, and industrial production relations are not regulated by specification.^{*11} Nevertheless, it is an institution that still cannot be avoided in present-day society.^{*12} The turning point in the formation of this institution in the Baltic territories came during the period under investigation in this article.

First, the article gives a general overview of the institution of specification in 19th-century Europe. Then the regulation of specification in the Baltic provinces before and after the application of the BES is analysed. The second section addresses both the draft of 1831 and scientific treatments. Next, the article analyses the provisions of the BES on production, comparing both existing regulation and contemporary examples. The subheadings proceed from the especially important features of the concept of specification provided by the BES. Finally, the article analyses the origins of the BES provisions and the models for them, seeking an answer to the question of whether there was only legislative fixation of the earlier law or, by contrast, the codification caused changes in respect of this institution.

1. The private law of the 19th century: From the specification of Roman Law to modern production

Specification involves a situation wherein one person has made something from material belonging to another person and the question is who has ownership of the new thing — the owner of the material or the producer. This is an institution that derived from Roman Law and was regulated by the norms of *ius commune* in the whole of Europe before the creation of modern private law codification.

Roman lawyers did not agree on the issue of specification at all. The viewpoint of the Sabinians was that the owner of the material — not the producer of the new thing (i.e., of the *nova species*) — was also the owner of the new thing. The Proculians held that the person who had given a new form to the material should be the

⁵ Bunge (1802–1897) studied at the University of Tartu (Dorpat at that time). Then, he was a private lecturer there between 1825 and 1830 and at the same time also a municipal syndic. In 1831–1842, he was a professor of provincial law at the University of Tartu. After that, he was a municipal syndic in Tallinn (then Reval) and was mayor and president of the Town Consistory. Between 1856 and 1865, he was a clerk in the Second Section, the codifying department, of His Imperial Majesty's Own Chancellery. After retirement, in the years 1869–1897, he lived in Gotha and Wiesbaden.

⁶ See M. Luts. Private Law of the Baltic Provinces as a Patriotic Act. – *Juridica International* 2000 (5), pp. 157–167; N. Reich. Kodifikation und Reform des Russischen Zivilrechts im neunzehnten Jahrhundert bis zum Erlaß des Svod Zakonov (1833). – *Ius commune* 1970 (3), p. 181 ff.

⁷ This expression is from H. Küpper. Einführung in die Rechtsgeschichte Osteuropas. Frankfurt/Main *et al.*: Lang 2005, p. 194.

⁸ F. G. v. Bunge (Note 3), pp. 25, 33, 36. See M. Luts. Die Begründung der Wissenschaft des provinziellen Rechts der baltischen Ostseeprovinzen im 19. Jh. – J. Eckert, K. Modéer (Hrsg.). Geschichte und Perspektiven des Rechts im Ostseeraum. Erster Rechtshistorikertag im Ostseeraum 8.–12. März 2000. Frankfurt/Main *et al.*: Lang 2002, pp. 161–167.

⁹ F. G. v. Bunge (Note 3), pp. 35–36, 39.

¹⁰ [F. G. Bunge.] Geschichte der Entstehung des Provinzialrechts. – Estonian History Museum (EAM), reserve 53, catalogue 1, item 49, [page 3 (*recta*)].

¹¹ O. Buccisano. Specificazione. Diritto privato. – *Enciclopedia del diritto*. Kd XLIII. Sospensione-Sviluppo. Varese: Giuffrè 1990, p. 276 ff.

¹² Production is included also to the Draft of the Common Frame of Reference. Book VIII Chapter 5, article 102. Draft of the Common Frame of Reference. TOM working group. Black Letter Text. Athens, 12 June 2008. (manuscript). The author expresses her gratitude to Professor Paul Varul for providing the manuscript for use.

owner of the new thing, also in the case in which materials of several owners were used. Justinian's codification applied (later *Corpus Iuris Civilis*) *media sententia*. If the new thing could be changed back into different materials (e.g., melting of a golden vase to form gold bars), the Sabinians' point of view was applicable. If such conversion was impossible (e.g., olive oil cannot be changed back into olives), the Proculians' point of view was applicable.^{*13}

In the tradition of *ius commune*, attempts were made to expand the provisions of Roman Law on specification, by means of different principles that were needed in practice (e.g., *bona fides*). Still today, researchers of Roman Law debate questions related to whether, according to Roman Law, also *bona fides* and the producer's will to acquire the thing were important. There is no agreement on the issue of whether the owner of the material has to be paid compensation in the case of acquisition of the thing by the producer.

Until the 19th century, a general conception, 'specification' (*specificatio*^{*14}), was used to denote this institution. With the attempts to codify private law, also practical needs were considered in relation to specification. To a considerable extent, the regulation of Roman Law provided certain limits and possibilities for interpretation that did not respond to the problems arising in practice (e.g., printing and taking photographs) anymore. Therefore, the compilers of the new bodies of codification wanted to eliminate the Roman opposition between *materia* and *species*. It was claimed that the work done by the producer is more important than that earlier opposition. Thus the principle of work was created, meaning that if the work of the producer is more valuable than the material of the other person, the produced thing should belong to the producer.

August Paret, who studied the development of the specification system up to the genesis of the German Civil Code (BGB), differentiated between the specification theories according to whether the theories consist of the 'principle of substance' or the 'principle of work'. He considered the Sabinians to be the representatives of the former and the Proculians the representatives of the latter.^{*15} Harald Elbert claims that the 'principle of work' was fully acknowledged in the 19th century, at the latest, and the historical school aimed to search for and find this principle also in the sources of Roman Law. He states that "[m]any intellectual attempts" were made to pass the formal considerations of Roman *media sententia* forward by retaining the solution of the sources but at the same time interpreting the 'principle of work' as a part of them. Although the sources did not provide the possibility for such interpretation, it was found that Roman practitioners of jurisprudence worked according to this principle but had not yet perceived it as a principle.^{*16}

The codification work of the modern age adopted the principles of Roman Law to a certain extent. The French *Code Civil* (1804) proceeded from the viewpoint of the Sabinians, according to which the owner of the material has the right to the new thing in the event of remuneration (Article 570).^{*17} The Austrian Civil Code (ABGB, 1911) joined the Sabinians' 'principle of substance', *media sententia*, and the 'principle of work' (§§ 414–415).^{*18} From the first codification onward, the General National Law for the Prussian States (1794; ALR)^{*19} applied the modern principles to production and withdrew from application of Roman principles most clearly. Here, in similarity to the conditions under Roman Law, the new thing has to have emerged in such a way that the material being used lost its current form and took a new one. If the producer has produced the thing in *bona fides*, the thing produced from the material belonging to another person remains in the ownership of the producer (Part 1, Chapter 9, § 304). The producer has to compensate the owner of the material for the material (Part 1, Chapter 9, § 302). Unlike in Roman Law, the new thing belonging to the producer does not depend on the ability for the new thing to be changed back into the materials used.

¹³ E.g., Inst. (*Corpus Iuris Civilis*) (CIC) part *Institutiones* 2.1.25., G. (textbook *Institutiones* by Gaius, a Roman jurist of 2nd cent.) 2.79., Dig. (part of CIC *Digesta*) 41.1.7.7. See H. Siimets-Gross, Scientific Tradition of the Roman Law in Dorpat: *usus modernus* or Historical School of Law? – Juridica International 2006, pp. 77–78 (with further references). Available at http://www.juridica.ee/international_en.php?document=en/international/2006/1/113248.SUM.php.

¹⁴ Roman jurists did not know the term *specificatio*. They used descriptions like: *Cum quis ex aliena materia speciem aliquam suo nomine fecerit* (if somebody makes a [new] thing out of the material belonging to somebody else in one's own name) or *Cum ex aliena materia species aliqua facta sit ab aliquo* ((Inst.2.1.25) if somebody makes something [new] out of the material belonging to somebody else) or asked simply a further question: *si ex uvis [...] meis vinum [...] feceris [...]* (G. 2.79) (if you make wine out of my grapes [...]).

¹⁵ A. Paret, Die Lehre vom Eigentumserwerb durch Spezifikation in ihrer Entwicklung bis zum Entwurf eines bürgerlichen Gesetzbuches für das deutsche Reich. Leipzig: Besold 1892, p. 6. The fact that the Proculians are the representatives of the principle of work, is not generally considered so natural. At the same time it can be said that the Proculians were the first who acknowledged the possibility to acquire things on the basis of specification, in which there is also a certain element of the principle of work. See H. Elbert, Die Entwicklung der Spezifikation im Humanismus, Naturrecht und Usus modernus. Inaugural-Dissertation zur Erlangung der Doktorwürde einer Hohen Rechtswissenschaftlichen Fakultät der Universität zu Köln. Manuscript. Köln 1969, p. 60.

¹⁶ H. Elbert (Note 15), pp. 61–62.

¹⁷ Here and hereinafter: French Code civil at http://www.legifrance.gouv.fr/affichCode.do?sessionId=7113D1613ABEF219BAFF1B62ADA0D2F6.tpdjo06v_3?idSectionTA=LEGISCTA000006150116&cidTexte=LEGITEXT000006070721&dateTexte=20080507 (7.05.2008). These provisions have been changed with the act No. 60-464 of 17 May 1960, but only with regard to the provisions of remuneration.

¹⁸ Here and hereinafter: Austrian Allgemeines Bürgerliches Gesetzbuch at <http://www.ilibio.org/ais/abgb2.htm#t4> (5.05.2008).

¹⁹ Here and hereinafter: Allgemeines Landrecht für die Preussischen Staaten von 1784. Mit einer Einführung von dr. H. Hattenhauer und einer Bibliographie von dr. G. Bernert. 2nd expanded edition. Neuwied, Krefeld, Berlin: Luchterhand 1994.

There was desire to communicate the new essence with new concepts, which were brought into use also in scientific literature. In the German cultural space, the ‘principle of work’ was conveyed by means of a new concept, which is demonstrated by the word choice directed to the activity: e.g., *Formgebung* (shaping)^{*20}, *Umformung* (reshaping)^{*21}, *Verfertigung* (producing).^{*22} In the draft of the Baltic private law codification of 1831, both the new and the old concept were used, in parallel: “*Umwandlung* [transformation] *oder Specification*” (§ 982), henceforward also the concepts of *Verfertigung* (§ 984) and *Verarbeitung* (§ 987).^{*23} Finally, the German BGB^{*24} started to use the concept of *Verarbeitung oder Umbildung* (production or reshaping).^{*25} The BES applied the idea of *Verarbeitung* (see Article 794), similarly to the ALR, the ABGB (§ 414), and the Saxon Civil Code (1863), which had done so before the BGB started to use it. The present article attempts to use a similar way of drawing a distinction — in discussion of Roman Law, the concept of specification is used; when the BES is discussed, ‘production’ is used.

2. The problem of specification in Baltic provincial law before codification

Before the BES entered into force in 1865, Roman Law was applied to specification in all of the Baltic Sea provinces in the form of *ius commune*.^{*26} Thus, the institution was affected not only by the interpretations of local lawyers but also by scientific literature from all over Europe. Nevertheless, in the present context the most important are the claims about local laws.

2.1. The draft of 1831 — retaining the solution of Roman Law

Between 1824 and 1840, Reinhold J. L. Samson von Himmelstiern^{*27} participated in several codification committees whose tasks were to prepare drafts of legislation. In 1831, the draft of the private law of the Baltic Sea provinces^{*28} was completed. Unfortunately, the draft has gone mostly unanalysed, but it was mainly Himmelstiern who compiled it. Although Himmelstiern’s draft never entered into force, it is still the first comprehensive treatise on the local private law, and one that could be relied on — also critically — in further scientific treatment of the local private law.^{*29}

In the draft of 1831, the following principles were important with respect to specification. Firstly, the produced thing does not have to be a completely new thing, but the characteristic shape of the thing or material must have changed (§§ 982, 985). Thus, as according to the Proculians’ viewpoint, the important factor is change of the shape. Secondly, *bona fides* is required, but it is not important with regard to the transfer of ownership. The transfer of ownership occurs also in the case of a *mala fide* producer, but said producer has to compensate for the value of the material to a greater extent (§ 987). The owner of the material has ownership over the material only if the produced material has been stolen (§ 986). Thirdly, the owner of the material has to be compensated in any case (§§ 987, 988).

Thus, the draft of Himmelstiern has not distanced itself from Roman principles, as under *media sententia* the owner does not lose the thing if its shape or form has not changed (§ 985). If the shape changes, the thing

²⁰ G. Hufeland. Institutionen des gesammten positiven Rechts. 2. Aufl. Jena: Akademische Buchhandlung 1803, p. 299.

²¹ C. F. Mühlenthal. Lehrbuch des Pandektenrechts. Nach der 3. Aufl. der Doctrina Pandectarum deutsch bearbeitet. 2. Theil. Halle: Schwetschke und Sohn 1836, § 248.

²² F. J. Stahl. Die Philosophie des Rechts. Bd. I. Tübingen: Mohr 1830, p. 300.

²³ [R. J. L. Samson von Himmelstiern] Darstellung des bürgerlichen Rechts der Ostseeprovinzen. 3. Volumes. [St. Petersburg] 1831.

²⁴ In case of BGB, here and hereinafter, the edition: Palandt Bürgerliches Gesetzbuch. 54. Aufl. München: Beck 1995; the institute of specification has not changed since 1900 when the BGB entered into force.

²⁵ H. Elbert (Note 15), p. 4.

²⁶ F. G. v. Bunge. Das liv- und esthländische Privatrecht. I Theil. Dorpat: Kluge 1838, p. 228; F. G. v. Bunge. Das curländische Privatrecht. Dorpat: Kluge 1851, p. 241.

²⁷ Himmelstiern (1778–1858) studied law at Leipzig; after that, he was a student teacher at the chancellery of the Livonian Landratskollegium, notary of the knighthood, assessor of the High Consistory, assessor of the Tartu County Court, member and president of the Livonian Court of Appeal, and land councillor. In 1824–1829, he was the president of the Committee for Livonian Provincial Laws; then, in 1829–1840, he was a clerk of the Imperial Chancellery’s codification department. He also helped to author the draft of a private law code and praised the codification of Roman law from Justinian’s time as something worth following. Source: M. Luts. Die juristischen Zeitschriften der baltischen Ostseeprovinzen Russlands im 19. Jahrhundert: Medien der Verwissenschaftlichung der lokalen deutschen Partikularrechte. – Juristische Zeitschriften in Europa. M. Stolleis, T. Simon (ed.). Frankfurt am Main: Vittorio Klostermann 2006, p. 80 ff.

²⁸ [R. J. L. Samson von Himmelstiern] (Note 23).

²⁹ M. Luts (Note 27), p. 93.

belongs to the producer. Thus it can be claimed that the draft was similar to and remained in the same tradition as the earliest codification attempts in German-speaking territories, such as the Bavarian *Codex Maximilianeus* (1756) and the Austrian *Codex Theresianus*, which was completed but remained a draft. Also these drafts proceeded from *media sententia*.³⁰ The draft of Himmelstiern included the condition of *bona fides*, but this fact did not change anything in the *media sententia* solution to ownership of the thing. The draft was concerned only with the amount of compensation, with the exception of things or materials that had been stolen. In this regard, the draft did not emphasise the ‘principle of morality’, which was very much praised by later lawyers in the BES.³¹ Also the ALR proceeded from “‘the principle of morality’, according to which nobody may acquire anything by illegal actions and enrich himself as a consequence of this”.³² In addition, the existence of the need for a *bona fide* producer (and thus for the obligation of compensation) to acquire a new thing was disputable under Roman Law. Contemporary authorities of Himmelstiern supported both viewpoints, and the earlier tradition supported the opinion that the need for *bona fides* was fundamental also under Roman Law.³³ Thus, the existence of the requirement for *bona fides* in the draft of Himmelstiern was in accordance with the opinions of at least some Romanists. The opinion that ownership of the new thing in the case of stolen materials belonged to the owner of the material was acknowledged even more universally.³⁴

Hence, if the draft of Himmelstiern had entered into force, the principles derived or deduced from Roman Law would have remained in force without any major changes. This conclusion is in accordance with previously expressed viewpoints about the draft of Himmelstiern and with his own opinion that the codification of the local private laws should be compiled on the basis of Roman Law.³⁵ This was exactly the case with specification.

Consequently, Bunge’s claim that Himmelstiern copied his draft from the ALR is not valid, at least with regard to this institution. The draft of 1831 is considerably different from the ALR. The concept of the new thing in the ALR (§ 304) is similar to the concept of the new thing in Roman Law and in the draft of Himmelstiern (§§ 982, 983), but according to the ALR, the producer will acquire the new thing only if having produced it in *bona fides* (I, 9, § 304). If the producer performs the work *mala fide*, he or she has to hand the new thing over to the owner of the material (I, 9, § 299). According to the draft of Himmelstiern, a *bona fide* or *mala fide* producer was not to have any influence on the ownership of the new thing; this factor influenced only the amount of compensation received by the owner of the material. Both Himmelstiern’s draft (§ 987) and the ALR (I, 9, § 302) provide that in the case of *mala fide* production, the owner of the material may demand the greatest possible compensation for the thing. The most important of these clauses concerns the question of who will acquire the new thing after production. With respect to this solution, the ALR and the draft of Himmelstiern differ from each other considerably. The similarity between the ALR and the draft of Himmelstiern with regard to the concept of the new thing derives from the general essence of the institution of specification, and therefore it existed already in Roman Law. The greatest possible compensation for the new thing in cases of *mala fide* production is a logically deductible punitive consequence.

2.2. Scientific treatments

Before the BES entered into force, specification had been studied scientifically by three lawyers in the Baltic Sea provinces. Carl Otto von Madai³⁶, a Romanist friend of Bunge at the University of Tartu, analysed two cases in his article of 1845. One case involved the following incident related to specification: a *bona fide* person has acquired a silver sheet and has transferred several pictures onto it, using daguerreotype. The former owner of the silver sheet demands the sheet back. In his analysis of this case, Madai asks whether it could

³⁰ H. Elbert (Note 15), p. 99.

³¹ C. Erdmann. System des Privatrechts der Ostseeprovinzen Liv-, Est- und Curland. I. Bd. Riga: S. Roderer Verlag 1889, p. 153; F. Seraphim. Zur Lehre vom Eigentumserwerbe durch Verbindung und Verarbeitung beweglicher Sachen nach dem Rechte der Ostseeprovinzen mit besonderer Berücksichtigung der einschlägigen Bestimmungen des Preussischen Rechts. Hamburg/Mitau 1881, p. 50.

³² H. Elbert (Note 15), p. 99.

³³ See, e.g., H. Elbert (Note 15), pp. 136–162.

³⁴ O. Meykow. Lehre des römischen Rechts von dem Eigentumserwerb durch Specification (1846). – Dorpater Juristische Studien. E. Osenbrüggen (Hrsg.). Dorpat: Verlag von E. J. Karow 1849, pp. 171–172.

³⁵ R. J. L. Samson von Himmelstiern. Codex der Livländischen Rechte nach der Römischen Pandekten-Ordnung. In: Jahrbuch für Rechtsgelehrte in Russland. Bd. 2. Riga 1824, p. 196–197. At the same time, Himmelstiern had the obligation to consider Roman Law only subsidiarily. See B. Dölemeyer. Das Privatrecht Liv-, Est- und Kurlands von 1864 (Teil III des Provinzialrechts der Ostseeprovinzen des Russischen Reichs). – Handbuch der Quellen und Literatur der Neueren Europäischen Privatrechtsgeschichte. III Bd. 2. Theilband. H. Coing (Hrsg.). München: Beck 1982, p. 2078. Since in relation to specification only the provisions of Roman Law were applicable, he did not contradict the requirements imposed on him.

³⁶ Madai (1809–1850) studied law at Halle and Berlin. Between 1832 and 1837, he was a private lecturer and extraordinary professor at Halle; in 1837–1837, he held a professorship in penal power, legal history, and legal literature at the University of Tartu; between 1845 and 1848, he held the title Professor of Roman Law at Kiel; and in 1848–1849 he was a member of the Frankfurt Parliament in the Paulskirche.

involve specification and refers back to the principles of Roman Law and *media sententia* (Inst. 2.1.25.).^{*37} Thus, Madai's analysis demonstrates that in the case of specification, Baltic private law had to proceed from Roman Law.

The other and the more thorough treatise on the specification problem was written by Ottomar Meykow^{*38} in the first half of the 19th century. Meykow, who held the title Professor of Roman Law at the University of Tartu, had written his candidate thesis on specification in 1846. Meykow studied the specification problem in Roman Law, which was, as already mentioned, applicable in the Baltic provinces in the form of *ius commune*. The purpose of the thesis was to make suggestions as to how to interpret the applicable law and thereby offer solutions to the situation in the local provinces with regard to this question (he never stated the latter), at the same time remaining within the framework of Roman Law. Bunge, the compiler of the BES, commented on the course of the compilation by saying that the notes of Meykow on Roman Law were especially valuable for him and therefore he took them into consideration.^{*39} The present article attempts to answer the question of whether he did this also in the case of specification.

In the context of the present article, two problems from Meykow's paper 'Die Lehre des römischen Rechts von dem Eigenthumserwerb durch Specification'^{*40} are important. Firstly, did Roman lawyers consider *bona* or *mala fides* important when determining the status of the new thing, according to Meykow? Secondly, Meykow studied the issue of whether, for acquisition of ownership of the new thing, the will (*die Wille*) of the producer was important.^{*41} Meykow paid little attention to whether the thing had to be *nova species* (which was stressed both in Roman Law and in the ALR). He discussed this issue in only one place and again in relation to the will of the producer to acquire the new thing; in this case, the thing has to be *res nullus*. According to *media sententia*, the thing did not belong to anybody in the event that the material that was used to produce the thing could not be changed back.^{*42} Thus, according to Meykow's viewpoint (which follows *media sententia*), a thing can be described as a processed thing only if the material used cannot be changed back and therefore belongs to nobody. The producer can occupy and acquire the thing.

Meykow commented, on *bona fides*, that older practitioners of jurisprudence (from the glossators to the 19th century) believed that in Roman Law the necessary condition for acquiring a new, produced thing was a *bona fide* producer. Also modern lawyers wanted to see the principle of *bona fides* in the sources and thus, according to Meykow, wished subconsciously to develop Roman Law: "[T]hey have erred only in presenting the correct idea as a viewpoint of Roman lawyers *per se*. Namely, they felt the need for limiting the will of the producer with the moral power of *bona fides*"^{*43} — which was not actually there. Finally Meykow reached a conclusion that "although [...] *bona fides* of the producer is not necessary for acquiring the produced thing, the modern lawyers have not wished to acknowledge the sentence, with all of the consequences deriving from this". Namely, some modern lawyers acknowledge the particularity of the stolen thing because it cannot be acquired in property via production.^{*44} More than 100 years later, Elbert agreed with Meykow's conclusions about the absence of *bona fides* and interpretation of the current tradition.^{*45} Thus, Meykow found differently from the provisions of the ALR that according to Roman Law *bona fides* was not necessary.

Meykow did not think that the producer should be accountable for the disappearance of the old thing by production — as a *bona fide* owner should not be accountable for the disappearance of the thing owned by him or her. The analogy between a *bona fide* owner and a producer is said to be denied by most lawyers, and, regardless of *bona fides* of the producer, they have found that the producer has to compensate the owner of the produced material in an extent corresponding to the extent to which said producer has enriched him- or herself in consequence of this (Dig. 50.17.206; 6.1.23.5.). Meykow believed that the sources of Roman Law

³⁷ C. O. v. Madai. Rechtsfälle: II. Das Daguerrotypbild. – Theoretisch-practische Erörterungen aus den in Liv-, Esth- und Curland geltenden Rechten. IV Band. Dorpat 1845, pp. 94–96.

³⁸ Meykow (1823–1894) studied in the Faculty of Law at the University of Tartu between 1842 and 1845. In 1846, he wrote his thesis as a candidate for a master's degree; in 1847, he received his MA; and he was granted a PhD degree in 1850, also at Tartu. In 1855–1857, he was an extraordinary professor in Kazan, and between 1858 and 1892 his main work was in the professorship of Roman Law at the University of Tartu.

³⁹ [F. G. Bunge.] (Note 10), [I. 5]. According to Dölemeyer, Meykow participated in the work of the Second Section, or codifying committee, of His Majesty's Own Chancellery during the final redaction of the draft of the BES. See B. Dölemeyer (Note 35), p. 2080.

⁴⁰ O. Meykow (Note 34), pp. 152, 166–167.

⁴¹ H. Siimets-Gross (Note 13), p. 80. Elbert considered important to highlight the four main elements when treating the historical evolution of specification: the concept *nova species*, the principle of work as the basis for acquisition, the demand for *bona fide* and the condition of *suo nomine*. H. Elbert (note 15), p. 2. The condition of *suo nomine* is connected to the Meykow's issue of the will; also Elbert refers repeatedly to Meykow (e.g., p. 56 ff).

⁴² O. Meykow (Note 34), p. 173.

⁴³ *Ibid.*, p. 168.

⁴⁴ O. Meykow (Note 34), pp. 171–172.

⁴⁵ Referring in his conclusions also to Meykow. H. Elbert (Note 15), p. 137, not for example H. Dernburg, who still found that already in Roman Law *bona fide* was a necessary factor (D. 10.4.12.4). This sufficient and practical idea was included into the ALR. H. Dernburg. Das Sachenrecht des Deutschen Reichs und Preussens. Halle: Verlag der Buchhandlung des Weisenhauses 1898, p. 299.

that are shown as the basis are too general or address *accessio*^{*46} cases and therefore cannot be applied to specification.^{*47} Therefore, according to Meykow, Roman Law does not require any compensation from the *bona fide* producer (differently from the ALR).

According to Meykow, most researchers think that the question of changing back the produced thing may be subject to discussion only if the produced material belonged completely to somebody else. If the producer produced partly his or her own and partly somebody else's material, the thing belongs in every case to the producer (on the basis of Inst. 2.1.25).^{*48} Nevertheless, it was said to disagree with two fragments of digests (Dig. 6.1.5.1 and 41.1.12.1) and the principle of reasonableness, as in this case even a minimal amount of the material belonging to the producer among a large and valuable amount of material can mean that the thing belongs to the producer, without any further argument.^{*49} Meykow believed that these two cases — when the thing is completely of material belonging to somebody else or partly made from material belonging to the producer — cannot be separated from each other (as in the ALR).

Therefore, Meykow's aim was to purge the applicable Baltic private law, or Roman Law, of certain false conclusions on *bona fides* and on compensation for the material used.

The third author of scientific treatises addressed here is Friedrich Georg von Bunge, the author of the BES draft. Bunge notes in his treatises on the applicable laws in Livonia, Estonia, and Curonia that "receiving the right of ownership by using the *accessio* and specification, the provisions of Roman Law are applicable".^{*50} Additionally, Bunge highlighted an exception to the Livonian chivalric law, which allegedly derived from the Saxon law: "[T]he person who ploughs a field that belongs to another in *bona fides* will lose the worth of his work if an action is filed before the seeds are sown; if the seeds are sown before filing of an action, the plougher will get the crop and will pay the compensation to the owner of the field for using it."^{*51}

All lawyers who tackled the problem of specification — Madai, Meykow, and Bunge, who later compiled the BES — have not mentioned that treating *specificatio* according to Roman Law could be outdated or not in compliance with the private law applicable in the Baltic provinces. On the contrary, in the second publication of 'Das liv- und esthländische Privatrecht' ('The Private Law of Livonia and Estonia') of 1851, Bunge clearly noted that Roman Law is applicable.

3. Production in the BES

3.1. The general concept

The most important norm of the BES related to production is Article 794:

Wenn durch kunst- oder handwerksmässige Verarbeitung fremden Materials im guten Glauben eine neue Sache dergestalt gewonnen worden, dass die dazu verbrauchten Materialien ihre bisherige Form verloren und eine neue Gestalt angenommen haben, so wird die neue Sache, ohne Rücksicht darauf, ob die fremden Materialien daraus abgesondert werden können oder nicht, Eigenthum des Verarbeitenden. Dieser muss aber den Eigenthümer des fremden Materials in der im Art 792 angegebenen Weise entschädigen.^{*52}

The provisions of Articles 791–792 and 795–798 are also applicable to production.

^{*46} As a result of *accessio* two things, which can belong to different owners, merge or are joined. Often one of the things can be considered an accessory thing and in this case the accessory thing is joined with the principal thing. If the accessory and principal things cannot be separated, the joined thing is in common ownership of the former owners.

^{*47} O. Meykow (Note 34), pp. 180–182.

^{*48} *Ibid.*, pp. 175–176.

^{*49} *Ibid.*, pp. 177, 179.

^{*50} F. G. v. Bunge, 1838 (Note 26), p. 228; F. G. v. Bunge (Note 4), pp. 281–282; F. G. v. Bunge, 1851 (Note 26), p. 24. With regard to the applicability of specification Bunge referred to Madai's asserting opinion in the second publication of "Privatrecht". See F. G. v. Bunge (Note 4), pp. 281–282.

^{*51} F. G. v. Bunge, 1838 (Note 26), p. 228; F. G. v. Bunge (Note 4), pp. 281–282. Bunge gives a similar exception of sowing crop also in relation to Curonian law. F. G. v. Bunge, 1851 (Note 26), p. 241.

^{*52} When a new thing emerges after *bona fide* production of material belonging to somebody else in an artistic way or via handicraft and the materials used for this lose their current form and take a new shape, the new thing will be the possession of the producer, whether materials belonging to somebody else can or cannot be separated. The producer has to compensate the owner of the material in a manner set forth in Article 792.

3.2. The new thing

According to Article 749, it is important that the new thing have been produced from material belonging to somebody else in such a manner that the materials being used have lost their former shape and are reshaped. The same is provided by the ALR but not word for word (I., 9, § 304) and is, according to Roman Law and the essence of the institution, the common element of the majority of the norms in need of updating. Carl Eduard Erdmann^{*53} indicated that in the case of the BES regulation, the origination of the new thing (*nova species*), which was the presupposition in Roman Law, was not important anymore. In decision as to whether a case involves specification or not, the important factor is whether the work is done in an artistic way or by handicraft: “With this, the work is acknowledged as the actual basis for acquisition.”^{*54} Thus Erdmann did not directly deny the fact that during production a new thing will emerge, but he considered this unimportant to such an extent that it seems he did not consider the existence of a new thing necessary.^{*55}

Differently from Erdmann, Seraphim stressed the importance of the new thing: “The essence of production is the emergence of a **new** thing that can be denoted with **another concept** and which is a result of work of one person. The provincial law is in accordance with Roman Law when setting conditions according to which *nova species* has to emerge.”^{*56} This does not change Erdmann’s conclusion according to which the important basis for acquisition in the BES is work. In Article 794 of the BES, the emergence of a new thing is very important by all means, and to it another condition has been added. Namely, this new thing may be only a result of artistic work or handicrafts. If there is no new thing, the provision is not applicable.

According to the BES, differently from Roman Law (see D. 41.7.7), whether the material belonging to another person can be separated or not is unimportant (the possibility of separation matters only in the case of *mala fide* production, according to Article 791).^{*57} These circumstances expand the concept of production in the BES such that Article 794 can be applied to some cases that did not belong to the specification concept in Roman Law (or to cases that were not acknowledged as specification), like painting, photos, and daguerreotype.^{*58} Under Roman Law, in the case of the above examples, the former state of the material used could be restored — by washing the canvas or cleaning the silver plate — and thus the material belonging to another person did not change and remained with its former owner, even though the addition could have increased the value of the material substantially.

Meykow believed that according to Roman Law, the cases in which the thing is completely of material belonging to another person or partly of material belonging to the producer cannot be isolated.^{*59} The BES did not provide for this. The last statement applies not only to the narrow regulation on production in the BES but also to acquisition of the new thing that has emerged without artistic work or handicraft and which is regulated by Article 792. In Roman Law, this case was also regulated by provisions applying to specification. In the BES, the case described was regulated on the basis of joining and mixing, and therefore the provisions on production did not apply to it. Perhaps one can consider the indirect influence of Meykow here in the fact that the most important reproof by Meykow is prevented. According to Meykow’s reproof, the interpretation can be that also a minimal amount of material belonging to the producer among a large and valuable amount of the produced material can mean that the thing belongs to the producer, without any further argument.^{*60} It may be because of this that Article 792 of the BES stresses that the new thing that has emerged is property of the person who has produced it only if this person has undoubtedly added most of the material as judged by value.^{*61}

⁵³ Erdmann (1841–1898) began his studies at the University of Tartu in 1858, at first in philosophy and then in law. Then he started his studies at Heidelberg University. Between 1864 and 1869, he was an assistant secretary and the secretary of the Mitau (the present Jelgava in Latvia) town council. In 1869–1873, he was a solicitor for the University of Tartu. Partway through that time, in 1870, he defended his MA thesis. In 1870–1872, he was a private lecturer at the University of Tartu. Then, in 1872, he received his PhD; in the same year he became an extraordinary professor. A year later he became an ordinary professor. In 1893, he was dismissed and retired.

⁵⁴ C. Erdmann (Note 31), p. 154.

⁵⁵ Still, the demand for the new thing exists and thus important both in the BGB and Estonian Law of Property Act (Asjaõigusseadus. – RT I 1993, 39, 590 (in Estonian)).

⁵⁶ The text shows Seraphim’s spacing. F. Seraphim (Note 31), pp. 43–44.

⁵⁷ Both C. Erdmann (Note 31), p. 154 and F. Seraphim (Note 31), p. 41. According to the ABGB, the materials have to be changed back if possible, similarly to Roman Law. Also Ursula Flossmann thinks that by regulation specification in the ABGB the principles of *ius commune* have been followed. U. Flossmann. *Österreichische Privatrechtsgeschichte*. Wien–New York: Springer 1983, pp. 163–164.

⁵⁸ F. Seraphim (Note 31), pp. 50–51. Compare C. O. v. Madai (Note 37), pp. 94–96.

⁵⁹ O. Meykow (Note 34), pp. 175–179.

⁶⁰ *Ibid.*, pp. 177, 179.

⁶¹ Deciding on the value of the thing in this way is usual in the codifications of the 19th century, also in *Code Civil* (Articles 568, 569), ALR I, 9, § 307, BGB § 950.

3.3. Production in an artistic way or by handicraft

According to the BES, the new thing has to emerge in an artistic way or by handicraft (being so in clear opposition to the cases regulated by Article 792). According to Erdmann, production in such a way presumes that the producer has special technical knowledge (thus the possibility of accidental emergence of a new thing is excluded). Whether the new thing has emerged in an artistic way or by handicraft is a decision of the judge of a single case. Erdmann gave an example of a herdsboy with a willow whistle. Here the question is to what extent artistic production can be confirmed.^{*62} Seraphim noted that also it is unimportant that the result of the work is in compliance with all ‘rules’ of the craft concerned or the corresponding art field, and these concepts in this context should be interpreted in the broadest sense. One definitely cannot proceed from the status of the producer with respect to being a professional artist or artisan.^{*63}

Also this condition highlighted by the BES commentators derives indirectly from the ALR. Roman Law had no such condition. Still, the condition in the ALR was not a part of the production concept, but it explained the concepts of joining and mixing: “Hat jemand ohne kunst- oder handwerksmässige Verarbeitung, fremde Materialien mit den seinigen, jedoch nicht betrüglicher Weise, verbunden, vermengt oder vermischt [...]”^{*64} However, the BES presents this condition as one part of the general concept of production. The present study cannot answer the question of whether production in an artistic way or by handicraft could (although not mentioned in the ALR) fall under the idea of the ALR provision (I., 9., § 304) or a wider interpretation given to the provision later and added to the BES on the basis of the theory of law. When answering the question “what does it mean — reshaping?”, F. Förster noted that “this is not a legal but an economic question; this should be answered by industry, and the answer should be that the product emerging as a result of the work has to have a different value”.^{*65} With the condition of production in an artistic way or by handicraft, the BES has given production a completely different content when compared to all other contemporary legislation. Neither the ALR nor other legislation that preceded the BES included such a condition (for example, the ABGB and the French Code Civil). Also legislation contemporaneous with the BES does not include the condition.^{*66}

Because of this specific addition — the emergence of a new thing only through production in an artistic way or by handicraft — several typical cases, like crushing grapes or joining melted metals without any artistic or handicraft knowledge, which according to Roman Law involved specification, are excluded. Thus, the concept of production in the BES is much narrower than it was in Roman Law. In the case of melted metals, Article 792 (if the new thing is more valuable than the material, which is unlikely in the above-mentioned example cases) or Article 793 (for cases wherein the owner has the right to choose whether to acquire the thing or demand compensation) of the BES is applicable. At the same time, the condition of these two articles is that different materials have been joined (*Verbindung*), mixed (*Vermengung*), or melted (*Vermischung*). It is my belief that, for example, extracting juice from apples does not belong to any of these classes. On the other hand, there is a new thing that is not apples anymore and that cannot be changed back into apples. At the same time, extracting juice from apples does not require special knowledge.

3.4. The condition of *bona fides*

According to Article 794, the existence of *bona fides* is necessary. According to Article 791, in the case of *mala fide* production, the owner of the material has the right to demand ownership of the new thing (thus excluding the possibility of acquiring the thing through specification) without any compensation for the work and the material belonging to the producer or demand compensation for the highest value of his or her material in addition to loss of profit and other loss. Thus we can agree with Erdmann’s viewpoint, according to which, pursuant to the BES, acquisition of the thing through specification is possible only in the case of *bona fide* production.^{*67} Seraphim stressed the principle of *bona fides* even more: “Provincial law differs from Roman Law fundamentally because the most important factor in it is **the principle of morality** and the result of the work can be **acquired only by a bona fide producer**.”^{*68}

⁶² C. Erdmann (Note 31), pp. 154–155.

⁶³ F. Seraphim (Note 31), pp. 48–49.

⁶⁴ ALR Part I, Chapter 9, § 307: “If somebody has merged, mixed or combined the materials belonging to somebody else without production in an artistic way or by handicraft but not in *mala fide*...”.

⁶⁵ F. Förster. *Theorie und Praxis des heutigen gemeinen preussischen Privatrechts auf der Grundlage des gemeinen deutschen Rechts*. 4. Aufl. III Bd. Berlin: Reimer 1883, p. 229.

⁶⁶ E. g., Saxon ABGB. Article 468 of *Codice civile del Regno d’Italia* of 1865 noted that “if an artisan or other person makes...”, but it actually means that it was not important if the maker was an artisan. In addition, the article did not mention anything about the way of production. See A. Paret (Note 15), pp. 43, 62.

⁶⁷ C. Erdmann (Note 31), p. 153.

⁶⁸ Spacing by Seraphim. F. Seraphim (Note 31), p. 50. In addition to Seraphim’s spacing, the expression “the most important factor” has to be stressed. Namely, Seraphim finds that although in Roman Law the producer had to work also in *bona fide*, this is not so important there as it is in the provincial law.

The question of whether the producer had to be *bona fide* also in Roman Law is arguable^{*69} and it was subject to debate also in the 19th century. As Seraphim followed in this respect those who believed that the producer had to be *bona fide* also in Roman Law^{*70}, then Erdmann found that, according to prevailing opinion, the necessity of a *bona fide* producer was not fundamental in Roman Law.^{*71} The existence of *bona fides* in Roman Law was addressed also by Meykow, who believed that Roman Law did not require *bona fides*. This belief is commonplace also today. Still, the solicitors of the first half of the 19th century held the opinion that the producer has to compensate the owner of the material used to the extent to which he or she was enriched^{*72} and at least in this respect the principle of *bona fides* was issued from.

On the occasion on which responsibility obtains, the BES proceeded from the opinion of those lawyers with whom Meykow did not agree. According to this opinion, the producer has to compensate the owner for the material he or she has used (see Articles 792, 793, 794, etc.). Thus the BES did not apply the analogy between the *bona fide* producer and the owner, which was preferred by Meykow; it instead proceeded from the general principle of Roman Law — “*iure naturae aequum est neminem cum alterius detrimento et iniuria fieri locupletiores*” (Dig. 50.17.206), which Meykow held to be so general that no conclusions can be drawn.

The requirement of a *bona fide* producer is set forth by the ALR similarly to the BES (I, 9, § 304) — a *mala fide* producer will not gain ownership of the thing. In this respect, the ALR and BES differ from the draft of 1831, the ABGB, and the French Code Civil.^{*73}

Paret categorised the BES as a codification that “follows the principle of work but [in which] the acquirement of the thing by the processor is dependent on the *bona fide* conditions”.^{*74} Here, Paret noted that the BES has the same standpoint as the Prussian ALR: “Also the Prussian ALR assigns ownership of the new thing to the producer on the condition that the producer is *bona fide* and regardless of whether the thing can be changed back or not.”^{*75} For Paret, the most important concepts of the BES were *nova species*, *bona fide*, compensation for the value [of the material used], and whether the thing can be changed back.^{*76}

At the same time, he did not comment on the change of the concept of specification in the BES — namely, that the term ‘production’ in the BES means only production in an artistic way or by handicraft.

In his treatise on the BES, Seraphim highlighted an additional feature — only at the beginning, when discussing the concept of production, without contemplating it later — that the producer, who produces the material belonging to somebody else, has to have the will to acquire the new thing.^{*77} This factor is not derived from the formulation of Article 794 directly (in co-effect with Article 792). We deal instead with the problems of the producer’s will as treated by Meykow (differently from some contemporary authors^{*78}) in relation to the case of Roman lawyers. Meykow also found this factor to be important.^{*79} Only Seraphim himself could have answered the question of whether he followed Meykow, pandect books, or Dernburg^{*80} when considering will important. The condition of production in one’s name has been set forth by earlier legal codes (the *Codex*

⁶⁹ See, e.g., H. Elbert (Note 15), p. 138 ff.

⁷⁰ F. Seraphim (Note 31), pp. 49–50.

⁷¹ C. Erdmann (Note 31), p. 153.

⁷² O. Meykow (Note 34), pp. 180–181.

⁷³ The need for *bona fide* is not clear also today. The BGB does not include the requirement for *bona fide* (§ 950) and since the ZGB includes it (Article 726), there have been many arguments about including or excluding the condition of *bona fide*. See further references H. Elbert (Note 15), pp. 136–137. Also, the Estonian Law of Property Act provides the principle of *bona fide*: “If someone processes a movable of another in good faith, the new thing belongs to the processor if the work is more valuable than the original thing, but otherwise to the owner of the original thing.”

⁷⁴ According to Paret, also the Bavarian Law and ALR belonged to these codifications, the same is said to be in effect in Württemberg. See A. Paret (Note 15), p. 47–51.

⁷⁵ A. Paret (Note 15), p. 49.

⁷⁶ *Ibid.*, pp. 49–51.

⁷⁷ F. Seraphim (Note 31), p. 37. C. Erdmann does not mention the will of the producer.

⁷⁸ E.g., D. I. A. Hellfeld. *Iurisprudentia forensis secundum Pandectarum ordinem in usum auditorii proposita*. D. G. E. Oeltze (ed.). Editio Quarta. Jenae: Officina libraria Crockeriana 1806, pp. 794–797; G. F. Puchta. *Cursus der Institutionen*. 2. Bd. 5. Aufl. U. Andorff (Hrsg.). Leipzig: Breitkopf und Härtel 1857, pp. 691–692. Differently, e.g., K. A. Vangerow. *Leitfaden für Pandecten. Vorlesungen*. Vol. 1. Part 1. Marburg/Leipzig: Elwert Verlag 1839, pp. 494–499. See H. Siimets-Gross (Note 13), p. 83–84. H. Elbert treats the condition of production in one’s name (*suo nomine*). See H. Elbert (Note 15), p. 163 ff.

⁷⁹ O. Meykow (see Note 34), pp. 152, 166–167. Although Meykow does not mention the condition of *suo nomine*, he could have derived the need for the producer’s will from the fact that the producer has to have the will to produce the thing in his or her name. If he or she produces the thing with the will to hand that thing over to somebody else, the owner of the thing will be someone else. The same applies in the interpretation of § 950 of the BGB. See BGB/Palandt (as cited in Note 24), p. 1144.

⁸⁰ Dernburg treats the case when the producer makes a thing to somebody else then the owner of the thing will be the employer. Also this situation is connected to the issue of the producer’s will, more specifically to make a thing for somebody else’s property. See H. Dernburg (Note 45), p. 300.

Maximilianeus and *Codex Thesianus*). The ALR, Code Civil, ABGB, BGB, and ZGB have abandoned this condition.^{*81}

It is surprising that two well-known lawyers interpreted specification under the BES, which actually is conveyed in only two articles, differently in several very important respects (namely, concerning the new thing and the will of the producer). At the same time, Erdmann, whose *System des Privatrechts der Ostseeprovinzen Liv-, Est- und Curland* was published later, did not give any further explanations of his viewpoint, different from Seraphim's^{*82}, although in the given situation this would have been not only reasonable but also essential in view of local legal practices.

Vladimir Bukovskij, who commented on the BES in 1914, mentioned neither of them. In addition to the text of the BES's Article 794, he highlighted only the aspect reflecting Erdmann's point of view — the importance of production in an artistic way or via handicraft by which the accidental emergence of a thing is excluded. Secondly, he highlighted the basis for differentiation of specification from merging and mixing^{*83}. The BES remained in force also after the First World War and until the Second World War. Contrarily to all previous jurisprudence, the civil law notes of 1939, which in their treatment of the emergence of a new thing follow the BES, do not mention the condition of production in an artistic way or by handicraft. Additionally, the *bona fide* condition and the obligation of compensation for the material are mentioned.^{*84}

4. The actual origin of the BES production institution and its model

Production was at variance from the principles of Roman Law as applied at the time already in the draft of the BES^{*85}, wherein articles 1025–1034 referred to a 'special memorandum' (*Besonderes Memoire*). On this, Bunge wrote the following: "B[unge] compiled about 20 memoranda on specific issues of private law that had to be decided on by legislators, and the majority of these were introduced to His Majesty the Emperor through the State Council to receive the Highest approval by the Highest."^{*86} On 2 July 1862, the emperor did approve several opinions he received through the State Council, among which was the 'special memorandum' (although with the wrong number), which was referred to in the treatment of specification in the draft BES. The reasoning provided for the opinion mentioned that in the compilation of the BES several changes were made, which were approved by the opinion.^{*87}

Therefore Bunge contributed also to departure from specification as it was under Roman Law for the rewriting of the BES. As mentioned above, the Roman variant of the BES was not codified. Yet still Bunge asserted the applicability of Roman Law in 1851, nine years before publishing the BES draft. In his paper of 1831, he stated that the pandect of local private law had to codify all applicable law "trustworthily and completely". Contrarily to the aim of gathering applicable law, in this case Bunge was personally the initiator of a fundamental change.

In his studies of the origins of rewriting the BES and the possibilities for its interpretation, Ferdinand Seraphim found that this material was adapted from the ALR^{*88}, which, in turn, gave a new form to Roman specification.^{*89} Seraphim's assertion that the BES rewriting provisions are very similar to the ALR is supported by the findings of the present paper. The solution of the BES is still quite different from the Roman handling of specification. Therefore, Bunge has achieved what he criticised Himmelstiern's draft of 1831 for — sometimes he did not compile existing local law but copied articles from the ALR (although not word for word).

^{*81} E.g., *Code Civil* regulates working in somebody else's name in other provision. H. Elbert (Note 15), pp. 172–173.

^{*82} Erdmann refers to Seraphim at the beginning of his specification treatment. However, he seems to reduce all the differences between their viewpoints to Seraphim's assumption that the ALR could be used as subsidiary source when interpreting the BES regulation. See C. Erdmann (Note 31), p. 153, Note 5.

^{*83} Bukovskij refers to Erdmann (Note 31), p. 154. V. Bukovskij. *Svod grazhdanskikh zakononij gubernij pribaltiskikh s prodolzheniem 1912–1914 g. I s razyasneniyami v 2 tomakh. Tom I.* Riga: G. Gempell 1914, p. 334.

^{*84} Civil Law. Notes under copyright. Compiled by A. Rammul according to the lectures by E. Ilus, Mag. iur. Tartu: Reta 1939, p. 212.

^{*85} Entwurf des Liv-, Est- und Curländischen Privatrechts. Provinzialrecht der Ostseegouvernements. 3. Theil. St Petersburg 1860.

^{*86} [F. G. Bunge.] (Note 10), [I. 3 (*versa*).]

^{*87} No. 38437. (Ijulja 2 = 2nd of July). Vysotshaishe utverzdennoje mnenie Gosudarstennavo Soveta. – Polnoje sobranie zakonov Rossiiskoi imperii. XXXVII vol. I. Section, 1862. No 37827–28621. Sankt-Petersburg 1865, pp. 599–600. By doing so, it was prevented the assessment of the BES as whole by the State Council in the question if it is in compliance with the general principles of the legislation of the Russian Empire (as the first and the second part of the provincial law were assessed). See B. Dölemeyer (Note 35), p. 2082.

^{*88} F. Seraphim (Note 31), p. 42.

^{*89} H. Dernburg (Note 45), p. 299.

5. Conclusions

The conclusions of this paper can be stated as follows. Firstly, in the case of specification, Roman Law was applicable in the Baltic provinces until 1865. The principles of Roman Law were followed also in the compilation of the draft of 1831. With respect to specification, Bunge's statement that Himmelstiern often based his codification on the ALR was not proved. It turned out that Himmelstiern remained true to his principles, according to which Roman Law should be the example in codification of local private law.

The second important conclusion is that the regulation of the BES as rewritten is not in compliance with the principles according to which the BES itself was required to be compiled. The law in use at the time (Roman Law) was not codified (as was done by Himmelstiern); instead, Roman Law was bypassed. Thus Bunge tried to prevent the influence of Roman Law and did so extremely successfully. He did not base his regulation of specification on the scientific papers of local lawyers or even on his own scientific treatises. In respect of this institution, Meykow's influence has not been proved; rather, the opposite is true. Bunge based his rewriting of the BES on the ALR (and not on the Code Civil or ABGB); i.e., he did what he criticised Himmelstiern for doing. The wording of the ALR was changed in the BES provisions, and substantial changes were made (e.g., with regard to production in an artistic way or by handicraft). Thus it was a conscious and active process in which the law applicable at the time was changed considerably.

One important conclusion that can be drawn from the present paper is this: no generalisations can be stated in response to the BES or the draft of 1831 — i.e., one may not claim that it was codifying only existing law. In relation to every single institution and regulation, one must ascertain what it is and whether it was used to curb the influence of Roman Law.^{*90}

⁹⁰ See also H. Siimets-Gross *Roman Law in the Baltic Private Law Act — Triumph of the Roman Law in the Baltic Sea Provinces? On the declining influence of Roman Law* – *Juridica International* 2007, pp. 180–189 (Available at http://www.juridica.ee/international_en.php?document=en/international/2007/1/131661.SUM.php). It highlights the general viewpoints of the 20th century according to which the BES is mainly based on Roman Law.



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Terminological Turn As a Turn of Legal Culture

1. Introduction

This article deals with the turning points in Estonian legal terminology in the transition from the Soviet era to the integration into Europe, considering the usage of Latin terms in juridical journals. Employing Latin terms is characteristic of European legal cultures and legal writings. The development of law in continental Europe has relied heavily on the Latin language and the system of concepts based on Roman law; historically, Latin has been extremely closely connected with the development of European law. In previous centuries, the bulk of legal literature and much legislation was compiled in Latin. Although Latin ceased to be the language of law and legal science in the 20th century, its significance as a technical means of communication among lawyers in Europe remains. The conciseness and linguistic economy of Latin terms encourages their use.^{*1} Precisely formulated Latin terms facilitate international communication of lawyers and enable them to exchange information and ideas effectively despite linguistic and cultural boundaries.^{*2}

Juridical journals have been chosen as the material for this research because periodicals are formally the most dynamic medium of law. According to M. Stolleis, in essence they could be called the ‘medial crossing-point’ where legal science, judicial and administrative practice, legal politics, and general politics meet.^{*3} Legal periodicals are a mirror of the legal culture.

It is obvious that different legal cultures shape very different journalism. Three major turning points and rearrangements in Estonian legal history in the course of the 20th century have had a strong impact on the legal culture and changed it considerably: 1918 with the creation of the Republic of Estonia, 1940 and 1944’s Soviet occupation, and the regaining of independence in 1991. At all of these points, radical legal reforms occurred.

¹ Typically juridical terms in Latin occur as single words — stem words and compound words, such as *usus* ‘usage, right of use’, *ususfructus* ‘usufruct’, or expressions, e.g., *bona fides* ‘good faith’. According to H. Saari, a term is a nominating linguistic unit, but not necessarily a noun. H. Saari. Omasõna ja võõrsõna paarid eesti oskussõnavaras (Native Word and Foreign Word Pairs in Estonian Terminology) (1). – Keel ja Kirjandus 1980/12, pp. 737–743. Thus, besides nouns, also verbs, adjectives, pronouns, numerals and adverbs can function as legal terms in Latin, for instance *non liquet* ‘it is not clear’, *bilateralis* ‘bilateral’, *ad hoc* ‘for this particular purpose’, *privatim* ‘in private’, *bis* ‘twice’, etc. As a rule, parts of speech other than nouns represent general language material which has acquired a specific meaning in professional context.

² N. Benke, F. S. Meissel. Juristenlatein. Lateinische Fachausdrücke und Redewendungen der Juristensprache, übersetzt und erläutert. Wien: Juridica 1997, p. 10.

³ M. Stolleis. Juristische Zeitschriften – die neuen Medien des 18.–20. Jahrhunderts. – Juristische Zeitschriften. Die neuen Medien des 18.–20. Jahrhunderts. Ius Commune Sonderhefte, Studien zur Europäischen Rechtsgeschichte, 128. M. Stolleis (Hrsg.). Frankfurt a. M.: Klostermann, 1999. p. XII: “... die Zeitschrift als ‘medialer Kreuzungspunkt von gerichtlicher und administrativen Praxis sowie von Rechtswissenschaft und Nachbarwissenschaften ...’”. Similarly, p. XIV: “Mit der Analyse einer Zeitschrift oder einer ganzen Landschaft von zeitschriften blickt man deshalb mitten in das tägliche Getriebe einer Rechtskultur”.

Against this background, the material collected during my survey reflects, in the context of Estonian legal history, the linguistic turning points: integration of one special language, legal language, into the European, then into the Soviet, and finally back again into the European legal environment. The present article focuses on the latter. The material for the study is composed of the content of two juridical journals published in Estonia: *Nõukogude Õigus / Soviet Law* (which was published from 1967 to 1989; in this article I have used the issues of the last five years of publication, 1985–1989) and *Eesti Jurist / Estonian Lawyer* (published from 1990 to 1994). Hence, the material covers equally five years of publication of both periodicals.

The aim is to ascertain whether the kind of revolutionary transformation processes that occurred within the legal order can be observed in legal terminology as well. Law is an area where the linguistic means of expression have a particularly great impact. This takes place through language, as a word or expression acquires juridical power. However, according to M. Aronoff⁴, a legal expression on its own or in a glossary is only an abstract item. Yet within a text it acquires a syntactic role and meaning. Therefore, just as legal periodicals reflect the legal culture, terminology also depends on the socio-cultural context, and terms are means to signify legal structures, relationships, values, and changes.⁵

The following questions are raised in this article: How are the changes introduced by the above-mentioned legal reforms mirrored in the usage of language by Estonian lawyers with regard to Latin terms? What is the moment in time that represents the return to the European legal environment in view of the usage of Latin terms in particular?

The hypothesis is that in the journals published during the Soviet era Latin terms are used less frequently. The juridical journalism of the Soviet time originated mainly with state administrative structures. That period established the Soviet system and Russian models: terminology was planned on the basis of the Russian language, and juridical texts and documents were translated from Russian.⁶ My hypothesis is also based on the fact that the majority of the authors of this time belong to a generation for whom classical studies were not officially available at Estonian universities. Study of the speciality of classical philology was abandoned at the University of Tartu in 1954 and resumed in 1990.⁷ Roman law was taught, but the academic research tradition in this field had been interrupted. Consequently, the knowledge of Latin held by many authors of legal texts of that time was inadequate and unsystematic.

The quantitative and qualitative method of study has been applied in my research; statistical data have been compared with a view to demonstrating dynamic changes.

2. Research material

Both periodicals, *Soviet Law* and *Estonian Lawyer* (until 1993), were published by the Ministry of Justice. It can be maintained that *Estonian Lawyer* developed from *Soviet Law*, because in 1990, when the new periodical began publication, the editorial board was not replaced and even the features and design of the journal remained the same. Both publications also had six issues per year.

The content of both periodicals was made up of the following features:

⁴ M. Aronoff. *Morphology by Itself. Stems and Inflectional Classes*. Linguistic Inquiry Monographs 22. Cambridge, Mass./London, England: The M.I.T. Press 1994.

⁵ N. Fairclough. *Critical Discourse Analysis*. London: Longman 1995, pp. 74–78.

⁶ H. Metslang. *Standard Estonian according to Area of Use: Problems and Solutions*. – *Operative language II. Essays on applied linguistics*. Tallinn: TPÜ Kirjastus 2004, p. 199.

⁷ It is impossible to give a clear answer to the question about the reasons behind closing down the Classics department at the University of Tartu during the Soviet period. Obviously, it was not done purely on ideological grounds, as Classics continued to be taught in universities in Moscow, Leningrad (St. Petersburg), Kiev and Tbilisi. Also in Lithuania, Classical studies were kept alive thanks to very strong cultural traditions. Classical philology did not pose a direct ideological threat, since it was not anti-Soviet. In Estonia, both subjective as well as local and objective reasons brought about the change. What was significant was that in studying and researching antiquity, it was possible to be directly in contact with western thought and culture. All similar fields of study vanished in Estonia during the Soviet time. Another significant cause was that within a limited range of means and possibilities first those subjects were closed which were considered to be dispensable because they seemed too impractical and not directly sympathetic to the ideological cause of the regime. The mentality of the lecturers was also considered inappropriate, as most of them had been educated during the time of the first independence. The circle of professors who taught Classics included those who actively resisted the Soviet regime, emigrated or died in the Second World War. A. Lill. *Kakssada aastat klassikalist filoloogiat Eestis: kahe alguse lugu* (Two Hundred Years of Classical Philology in Estonia: The Story of Two Beginnings). – *Kakssada aastat klassikalist filoloogiat Eestis* (Two hundred years of Classical Philology in Estonia). – *Morgensteri Seltsi toimetised I*. Tartu: Tartu Ülikooli Kirjastus 2003, pp. 11–12.

<p><i>Soviet Law:</i></p> <ul style="list-style-type: none"> – Each issue comprising about 75–80 pages – Articles (about 8–10, in total 24–37 pages, with an average length of around 2.5–4 pages) that are relatively short and rarely include an exhaustive analysis of the topic at hand – Information about dissertations defended and lists of names of students graduating from the Faculty of Law of the University of Tartu (1 page) – <i>In memoriam</i> items, obituaries, and memoirs related to lawyers who have died (4 pp.) – Reviews of national conferences in the USSR and travel accounts (3 pp.) – A glimpse at history (2–3 pp.) – Public prosecutor's supervision reports (1–4 pp.) – Economy and arbitration materials (2–4 pp.) – Reading for pleasure and juridical jokes (in total about a page per issue) – Bibliography (new legal literature and reviews of what was printed in various Soviet journals) (2–4 pp.) – Chronicle of events (in plenary sessions of the Supreme Court of Soviet Estonia, in the Ministry of Justice of Soviet Estonia, at the Prosecutor's Office of Soviet Estonia, and in the association of lawyers of Soviet Estonia, as well as jubilees of lawyers, 5–9 pp.) – New legal acts (decrees by the Presidium of the Supreme Council of Soviet Estonia on amendments to legislation/codes, regulations from the Council of Ministers of Soviet Estonia, and departmental regulations) (13–23 pp.) – Practice of the supreme courts of the USSR and the Estonian SSR (3–20 pp.) 	<p><i>Estonian Lawyer:</i></p> <ul style="list-style-type: none"> – Each issue comprising about 75–80 pages – Articles (about 7–8, totalling 35–40 pp., making the length of one article around 4–5 pp.) that, while fewer in number, are longer and thus more thorough – Information about dissertations defended and lists of students graduating from the Faculty of Law of the University of Tartu (1 page) – <i>In memoriam</i> materials, obituaries, and memoirs concerning lawyers who have died (1–2 pp.) – Reviews of conferences and interviews with foreign lawyers and jurists (2–3 pp.) – A glimpse at history (5–7 pp.) – Prosecutor's supervision materials (1–4 pp.) – Economy and arbitration (2–4 pp.) – Reading for pleasure (a short story about legal matters, 2–3 pp.) – Bibliography (new legal literature abroad, 1 page) – Chronicle of events and information (in the Ministry of Justice, at the Prosecutor's Office, in the Court of Arbitration, and from the Estonian Association of Lawyers, as well as related to jubilees of lawyers, 3–5 pp.) – International legislation (material on international conventions and agreements, 7–14 pp.) – New legal acts (decisions of the President, legal acts of the Republic of Estonia, and regulations of the Government of the Republic, totalling 12–20 pp.) – Practice of the Supreme Court (3–6 pp.) – Summaries in English (2 pp.)
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Formally, there does not seem to be much difference between the two periodicals, as both include similar topics and features. What sets them apart from each other are the content and ideology. The years under examination represent well the change in rhetoric: the 1985 *Soviet Law* commemorated the 45th anniversary of the creation of the Estonian SSR.⁸ The 1990 *Estonian Lawyer* dealt with the elapsing of 50 years from the Soviet occupation of Estonia.⁹ The history section of *Soviet Law* focused on the establishment of the Soviet legal system in Estonia, whereas *Estonian Lawyer* concentrated on the destruction of the courts administration of the Republic of Estonia in 1940. Owing to ideological factors, *Soviet Law* also addressed the problem of the struggle against alcoholism through history, which was a particularly important topic in 1985 because of the strict alcohol policy imposed by Gorbachev. *Estonian Lawyer* surveyed the history of the Faculty of Law of the University of Tartu, and published articles about famous Estonian lawyers of the pre-WWII period.

⁸ Nõukogude Õigus / Soviet Law 1985/3.

⁹ Eesti Jurist / Estonian Lawyer 1990/4.

As chances to get behind the Iron Curtain during the Soviet era were slim, visits abroad attracted great attention. Therefore, *Soviet Law* published interviews with those Estonian lawyers who on business trips had had the chance to spend time in foreign countries. Similarly, accounts were given of the meetings of the publication's board members with foreign visitors to Soviet Estonia (mainly from countries friendly to the USSR, such as Ghana).

Latin has been used only in articles and historical reviews here — i.e., in about half of the content. The remaining half, which distributes practical information and introduces new legal acts, as a rule contains no Latin terms.

What makes these two periodicals representative as linguistic objects of study is the fact that both have a broad circle of authors. Specialists in different legal fields published articles in them. Besides law professors, we can see among the authors also attorneys, prosecutors, and judges. The articles in both of the journals contain material concerned with all major areas of law and thus give an objective overview of the different aspects of terminology.

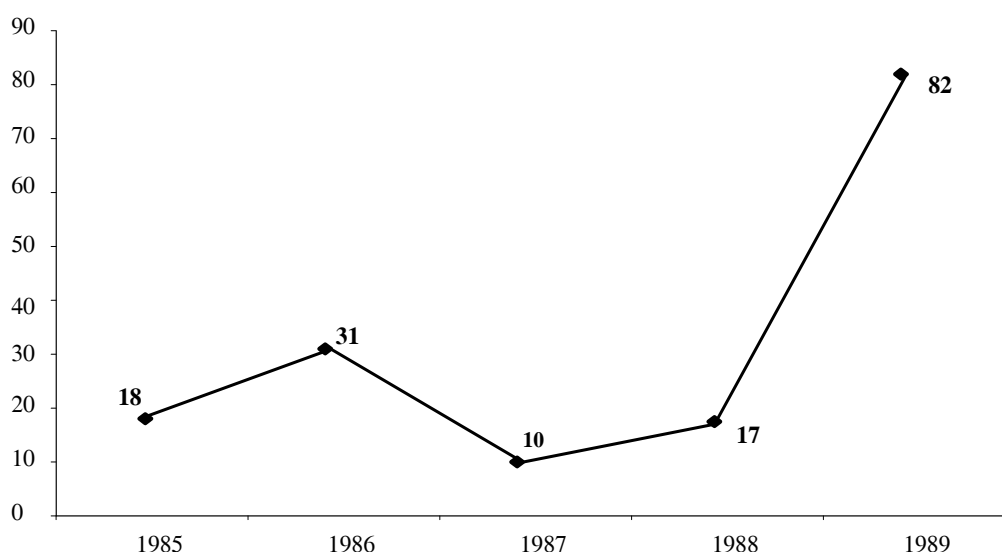
In 1993, a noticeable change occurred in *Estonian Lawyer*: it began to be published by the Association of Estonian Lawyers, the whole editorial board was replaced, the design was altered, and 12 issues per year began to be printed. The number of pages grew from approximately 480 to 750. Additionally, the whole concept was transformed: first and foremost, practical legal information began to be disseminated. The bulk of the content comprised legislative texts and commentaries on them, with articles now taking up only a third of the periodical. Besides the summaries of articles in English, synopses in Russian were provided. Overviews of court practice continued, and reviews of the legislation by ministries and local governments were added, as were chronicles of Riigikogu (Estonian Parliament) proceedings. Photos and other illustrative material appeared. Much space began to be devoted to the bibliography of new legal literature and reviews of articles on legal topics that appeared in Estonian newspapers. In 1995, *Estonian Lawyer* merged with *Juridica*¹⁰, the periodical published by the Faculty of Law of the University of Tartu, and the latter continues to be published to this day.

In total, my research dataset comprises:

- a) *Soviet Law*: five years of publication, 29 issues, 2380 pages
- b) *Estonian Lawyer*: five years of publication, 37 issues, 2920 pages

3. Frequency of usage of Latin terms

In total, Latin was used 158 times in five years in the articles in *Soviet Law*, thus, on average, 5.4 terms per issue. If we divide the number of pages by the number of terms, we can see that the Latin language appears on every 15th page of *Soviet Law*, on average. Quantitative changes in the usage of Latin terms in 1985 to 1989 are presented in Graph 1.



Graph 1: Latin terms in *Soviet Law*

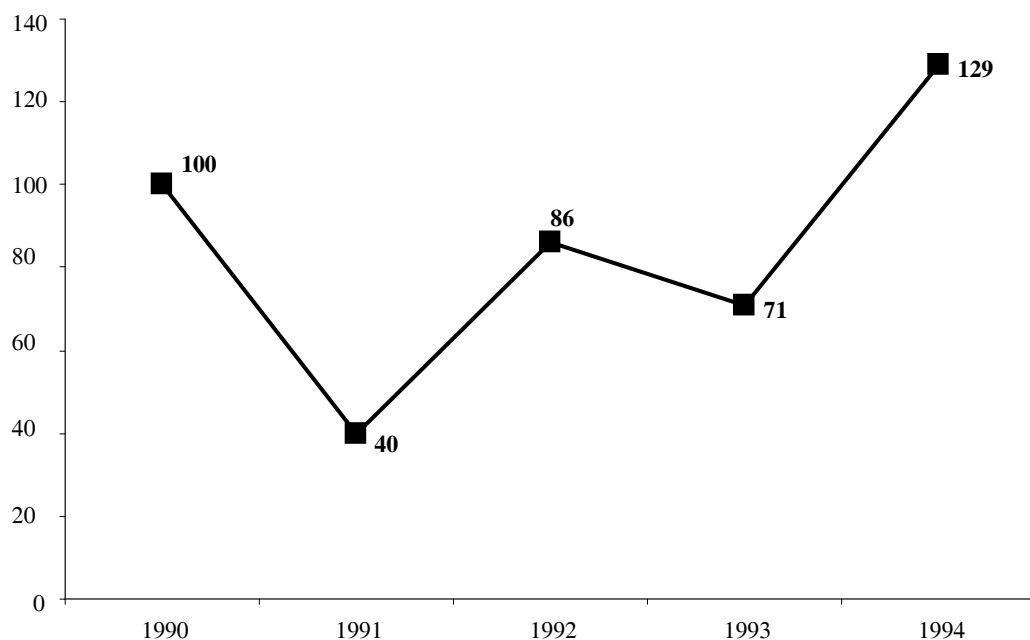
¹⁰ Juridica. Journal of the Faculty of Law of the University of Tartu. Editor-in-chief P. Varul. Tartu: Sihtasutus Iuridicum 1993–...

According to Graph 1, the usage of Latin terms increased noticeably in the last year of publication. In 1985, in total, 18 Latin terms were used. A year later, in 1986, in comparison, Latin terms were used 31 times already. For 1987, only 10 Latin terms can be found. In the next year, 1988, a slight rise again occurred: Latin terms were used 17 times. The biggest increase can be witnessed in the issues from 1989: Latin was resorted to 82 times in the course of the year.

What caused such large differences with regard to terminology? We can point out a significant detail here: up to 1989, no references to foreign-language sources were made in the articles. The majority of citations referred to Soviet authors and the ‘obligatory’ quotations from Lenin, Marx, and Engels. In 1989, scientific literary works in foreign languages became more readily available to Estonian lawyers, and several authors were able to go abroad. References to sources in English, French, and German in that year’s articles reveal that the authors were eager to study literature in other languages and to rely on a variety of foreign sources. Subsequently, the topics discussed began to change. Looking at the last years of *Soviet Law*, we notice that numerous articles in 1989 dealt with topics such as the possibility of self-determination, sovereignty, and international law (these years also mark the rediscovery of national identity and a resurgence of patriotism), which required more frequent use of Latin (e.g., in discussion of the sovereignty of the Republic of Estonia *de facto* and *de iure*). These trends continued in *Estonian Lawyer*, which began publication in 1990.

On the other hand, the abundance of Latin terms in 1986 and 1989 can be explained by the fact that in those years several articles appeared about the history of the University of Tartu, including the Faculty of Law. In historical references, a number of Latin expressions were used. In 1989, the 70th anniversary of the national university was celebrated.^{*11}

In the articles in *Estonian Lawyer*, Latin was used 426 times in total in the corpus — on average, 11.5 terms in each issue. If we divide the number of pages by the number of terms, we can see that Latin appears on every 6–7th page of *Estonian Lawyer* on average, twice as often as in *Soviet Law* (typically five expressions per issue and on every 15th page).



Graph 2: Latin terms in *Estonian Lawyer*

Graph 2 shows that the usage of Latin terms in the journal *Estonian Lawyer* over the years studied was more frequent in comparison with *Soviet Law*. In 1990, the topics of independence and internationalisation continued to be analysed, and, in total, 100 Latin terms were used. A year later, in 1991, Estonia regained independence. The journal mainly focused on distributing practical information: the changes in state structures and the release of new laws and regulations. As no Latin terms are used in Estonian legislation, and as the part of the journal that comprised articles was smaller in 1991, the number of Latin expressions used dropped — 40 instances can be counted. In 1992, Latin terms were used 86 times. For 1993, 71 Latin terms can be found. In the last year of publication, 1994, a remarkable 129 Latin terms were employed. It is impossible to cite any

¹¹ Even though the University of Tartu was originally founded in 1632, the anniversary of reopening the Estonian language based university in the first period of independence (1919) is celebrated separately. In earlier centuries, the language of instruction was Latin, German or Russian, depending on the scientific culture and political regime in the country.

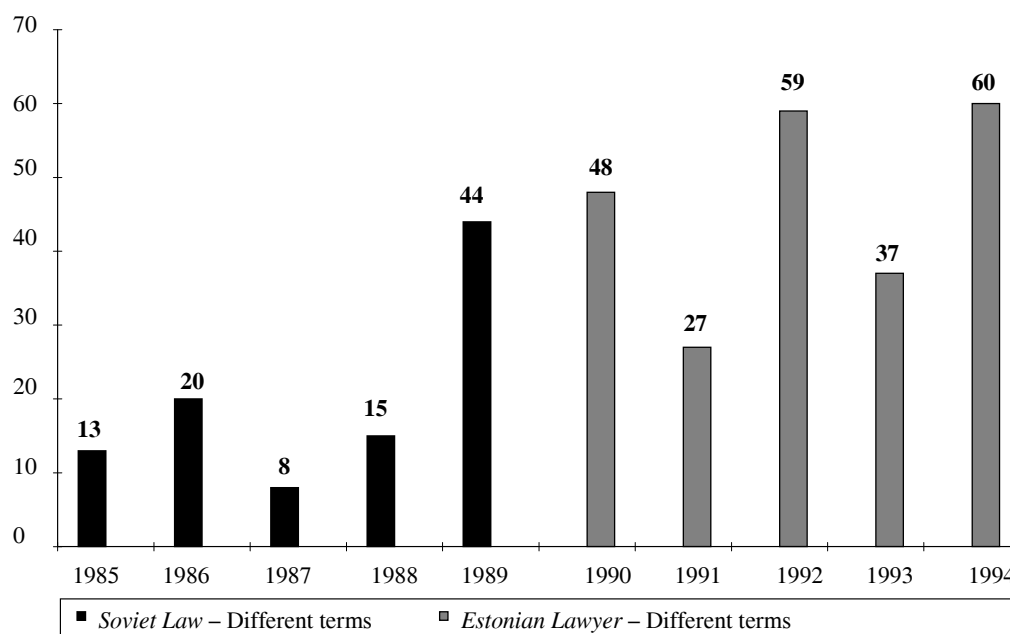
particular reason for this or refer to any specific theme; simply, many articles included Latin terms and this was becoming a natural part of juridical language use.¹²

It can be said that the juridical journal that appeared in Estonia after the collapse of the Soviet Union had to tackle a great reform assignment. The society was becoming oriented toward the West, and close contacts with the rest of the world were established. The system of concepts and the languages of influence changed — the importance of Russian as the source of reference diminished, and German and English became most influential instead.

Summing up the figures represented by both graphs, one can claim that, although officially Estonia regained independence in 1991, readiness to resume orientation toward Europe was clearly evident a few years earlier — in 1989 and 1990.

4. Lexical diversity and the most frequent terms

In addition to the perspective of their overall quantity, the Latin terms found in both journals can be compared from a qualitative point of view; i.e., I analysed the lexical diversity of the terms. In total, 65 different Latin expressions were used in *Soviet Law* in the course of five years, whereas in *Estonian Lawyer* twice as many — 128 — different terms can be detected.



Graph 3: Lexical diversity in *Soviet Law* and *Estonian Lawyer*

Graph 3 displays the usage of different terms in both periodicals by year of publication as analysed in the present article. In the second and last years of publication, the differences are not very noticeable: in *Soviet Law*, 20 different terms in 1986 and 44 in 1989, compared with, in *Estonian Lawyer*, 27 different terms in 1991 and 60 in 1994. Bigger qualitative changes can be observed in the first, third, and fourth years of publication. In the first year, 1985, only 13 different terms can be seen in *Soviet Law*, but in 1990 there were 48 terms in *Estonian Lawyer*. The third year showed even bigger differences: eight Latin terms in *Soviet Law* in 1987 but 59 in *Estonian Lawyer* for 1992. In the fourth year, the changes in terminological variety are not that dramatic in a comparison with the third year: 1988 showed 15 Latin terms in *Soviet Law*, and 1993 provided 37 in *Estonian Lawyer*. Accordingly, in addition to the quantitative differences between the two journals, a remarkable distinction can be observed in the variety and diversity of the terminology used.

¹² In the articles by Estonian lawyers today, many more Latin terms can be detected. The usage of Latin terms as expressions retaining the identity of European law has increased considerably in professional language in connection with legal reforms accompanying the accession of Estonia to the European Union in 2004. This has been analysed in more detail by M. Ristikivi in *Lexica iuridica in Juridica: Latin Terms as a Reflection of Europeanisation of Estonian Legal Culture*. – *Juridica International* 2007/12, pp. 173–179.

We notice that the authors in *Soviet Law* employ relatively modest usage of terminology in comparison with the language of the authors in *Estonian Lawyer*: Latin terms are fewer in number and less diverse: from 1985 to 1988, only 14 different Latin terms can be counted, on average, in the articles for the whole year (i.e., six issues in total, with around 450 pages in total). The main change occurred in 1989, when the terms grew in number: 44 different Latin terms per year. This indicates that the linguistic quality of legal texts improved in terms of variety and a more Western style of expression was adopted.

Semantically, we can divide all Latin expressions observed in both journals into three major classes: normative arguments that contain specific juridical information, terms used in rhetoric or for illustrative purposes (here belong mostly generally known Latin expressions and other widely employed maxims), and expressions pertaining to university and studies of law.

In both periodicals, the largest group is composed of Latin expressions as juridical arguments. In *Soviet Law*, of the 65 different expressions, 26 belong in this group; in *Estonian Lawyer*, 66 out of 128. About 40% of all Latin phrases in *Soviet Law* and 51.5% (i.e., about half) in *Estonian Lawyer* are used in their narrow juridical meaning.

The most frequent juridical terms are the following:

<p><i>Soviet Law</i>:</p> <p><i>de lege ferenda</i> — 6 times</p> <p><i>de iure</i> — 4</p> <p><i>ius gentium</i> — 4</p> <p><i>ex tunc</i> — 2</p> <p><i>ius est ars boni et aequi</i> — 2</p> <p><i>ius cogens</i> — 2</p> <p><i>vacatio legis</i> — 2</p>	<p><i>Estonian Lawyer</i>:</p> <p><i>de facto</i> — 23 times</p> <p><i>versus</i> — 16</p> <p><i>de iure</i> — 13</p> <p><i>de lege ferenda</i> — 11</p> <p><i>nullum crimen nulla poena sine lege</i> — 8</p> <p><i>lex</i> — 6</p> <p><i>fontes iuris</i> — 5</p>
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The most numerous among the expressions are terms related to legal theory, international law, penal law, and matters of sovereignty.

In addition to juridical terms, so-called juridical rhetoric is often used in articles — i.e., widespread Latin expressions and abbreviations. In both journals, such phrases make up about a quarter of all Latin expressions. I found 16 of these in *Soviet Law* (24.6% of the total) and 34 in *Estonian Lawyer* (26.5%).

<p><i>Soviet Law</i>:</p> <p><i>ca (circa)</i> — 15 times</p> <p><i>resp. (respective)</i> — 2</p> <p><i>tempora mutantur et nos mutamur in illis</i> — 2</p> <p><i>expressis verbis</i> — 1</p> <p><i>in medias res</i> — 1</p> <p><i>status quo</i> — 1</p>	<p><i>Estonian Lawyer</i>:</p> <p><i>ca (circa)</i> — 18 times</p> <p><i>etc. (et cetera)</i> — 7</p> <p><i>ex officio</i> — 4</p> <p><i>stricto sensu</i> — 3</p> <p><i>inter alia</i> — 2</p> <p><i>mutatis mutandis</i> — 2</p>
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Such expressions are ordinarily used in their general and neutral meaning in the articles. However, it is most difficult to draw a line between juridical argumentation and rhetoric in cases of terms that may acquire specific meaning in juridical contexts. A legal term might occur in legal language while also existing as a word in the common language, having a particular meaning there. Expressions like ‘*status quo*’ or ‘*inter alia*’ are of the kind used by lawyers in their general meaning but also used in a specific juridical meaning.

A considerable proportion of the Latin phrases used in the corpus examined here is made up of those employed in the corpus in descriptions concerning the history of the University of Tartu and the Faculty of Law. Please see the table below.

<p><i>Soviet Law</i>:</p> <p><i>stud. iur. (studiosus iuris)</i> — 17 times</p> <p><i>alma mater</i> — 11</p> <p><i>cum laude</i> — 11</p> <p><i>dr. iur. (doctor iuris)</i> — 11</p> <p><i>Album Academicum</i> — 7</p>	<p><i>Estonian Lawyer</i>:</p> <p><i>cum laude</i> — 35 times</p> <p><i>alma mater</i> — 14</p> <p><i>dr. iur. (doctor iuris)</i> — 12</p> <p><i>Academia Gustaviana</i> — 6</p> <p><i>studia iuridica</i> — 2</p>
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In *Soviet Law*, 23 such expressions could be found, remarkably accounting for 35.4% (a third) of all Latin phrases used. In *Estonian Lawyer*, 26 expressions (20% of the vocabulary) concerned the topic of university.^{*13}

The remaining 1.5% of the unique expressions in *Estonian Lawyer* comprised two medical terms: *in vitro* and *in utero*, which were published in 1993 in an article discussing the embryo protection act. This kind of term usage draws attention to the fact that technical language has its own characteristics setting it apart from general language. The neutral vocabulary of general language, legal terms, the technical terms of the particular fields involved, and the grammar of modern standard language constitute the instruments of legal language.^{*14} This means that legal texts have specific characteristics, yet, besides juridical terms, the terminology of the field that is the object of the particular legal text concerned, in addition to general language, has an effect on legal language.^{*15}

5. Comments and conclusions

Law is an area where linguistic means of expression are of utmost importance. The results of this survey draw our attention to the fact that language use is a social activity and the author of a text is part of that process. According to the creator of systemic functional linguistics, M. A. K. Halliday^{*16}, the author of a text uses language selectively for his purposes. In making linguistic choices — choosing words and terms, sentence structures, and other rhetorical systems — the author creates a text of certain characteristics and meaning. From the functional angle, writing a text is an instance of purposeful use of language, as in making linguistic choices the person considers the purpose and function of the text. The communicative function of language (the interpersonal meta-function) means that the author of an article uses language as a tool for presenting his own judgements, attitudes, and comments, and for creating a connection between himself and the reader.

The aim of my study was to investigate how the changes introduced by the legal reforms are mirrored in the usage of language by Estonian lawyers with regard to Latin terms. The research material consisted of periodicals whose authors are lawyers and whose function is to publish legal information for the readers, who are also lawyers. In the case of such specialised communication, the assumption is that the authors do not have to consider a target group of non-lawyers and thus can make use of technical terminology. However, the authors of the articles in both *Soviet Law* and *Estonian Lawyer* were rather modest in their usage of strictly juridical terms. More freely employed were expressions that are widely used also outside legal language and the vocabulary of the studies of law.

The statistical data analysed in the course of this research revealed that the usage of Latin terms in the juridical articles of 1985–1994 was directly connected with the socio-political changes that brought about extensive legal reforms. During the period investigated, new laws were drafted, and the legislation of European countries and international legal instruments were scrutinised. Reliance on European sources also influenced the usage of legal language. It is important to note that the quantitative and qualitative changes in language usage did not occur in 1991 — i.e., the year when Estonia restored her independence. The most significant changes in terminology had begun already in 1989 and 1990, when the readiness to try to become again part of the European legal environment surfaced. In a broader sense, it means that language usage must keep up with the developments in society. The legal environment changes; subsequently, language usage must change as well. Thus, the rearrangements in the Estonian legal system compelled the Estonian lawyers to include in their usage of legal language those Latin terms that have become rooted in the legal tradition of Europe.

¹³ Comparing the usage of Latin terms in the articles of the current authors we see that the greatest terminological change occurs on the qualitative plane. The research based on the 1993–2006 issues of the Estonian legal journal *Juridica* revealed that 732 different Latin expressions were used, the majority of which were strictly legal terms. A smaller group comprised Latin phrases and abbreviations also common in general language usage. Phrases pertaining to university studies are rather scarce in the writings by current authors, though. For more information, see M. Ristikivi, *Lexica iuridica in Juridica: Latin Terms as a Reflection of Europeanisation of Estonian Legal Culture*. – *Juridica International* 2007/12, pp. 173–179.

¹⁴ K. Kerge. Legal Language, Its Means and Prospects. – *Legal Language* 1995/4, p. 6.

¹⁵ R. Narits. The Methodology of Law I. Tallinn: Juura 1997, pp. 80–82.

¹⁶ M. A. K. Halliday. *Language and Society*. Cambridge: University Press 2007, pp. 195–197, 215–217.



The Council of the University of Tartu awarded at its 30 May 2008 session Professor Emeritus Werner Krawietz from the University of Münster the title of honorary doctor

Werner Krawietz was born in 1933 in Beuthen. From 1954 to 1960, he studied law, economics, philosophy, and sociology at the universities of Freiburg, Graz, and Münster. In 1960, he defended his doctoral thesis in economic and social sciences at the University of Graz and in 1965 his doctoral dissertation in law at the University of Münster. Also at the University of Münster he defended his *habilitation* degree work in 1974; he then worked there until 1979 with the title of Professor of Public Law, General Theory of Law, and Legal Philosophy. In 1979, he became the head of the Chair of the Sociology of Law and Legal and Social Philosophy. Then, in 1981–1982, he was the dean of the Faculty of Law of the University of Münster. From 1982 on, he was also a professor at the Central Institute of Spatial Planning at the University of Münster. Moreover, in 1982 he became a professor at the European Faculty of Sciences of Land Strasbourg. In 1990, the University of Helsinki awarded him an honorary doctorate. Later, in 1997, he became an honorary doctor also at the Russian Academy of Sciences. For many years, Krawietz has been deputy head of the German section of the International Society for Philosophy of Law and Social Philosophy. In 1974, he founded the journal *Rechtstheorie. Zeitschrift für Logik, Methodenlehre, Kybernetik und Soziologie des Rechts*, and since then he has been its publisher as well. After his retirement from professor's work in 1998, he continued his academic organisational activities and became director of the International Centre of German–Russian Legal Studies at the University of Münster. In addition, since 2002 he has been a member of the co-ordination committee of the German–Russian University Centre for Legal Studies Moscow.

Krawietz has been a highly productive scholar. The *Festschrift* volume *Theorie des Rechts und der Gesellschaft*, published in honour of his 70th birthday, contains a bibliographical annex that lists 357 publications. These include 42 monographs or parts thereof. His scholarly interest has been very broad, including questions of public law — in particular, constitutional law, the general part of administrative law, legal methods, theory of law and state, sociology of law (informational and communication theory as well as system and institution theory), and legal and social philosophy (especially philosophy of language, logic, and norm ontology and the field of behavioral and value theory).

The contact between Krawietz and the Faculty of Law of the University of Tartu was established in 1992, soon after Estonia regained its independence. He has visited Tartu many times and presented lectures to our students. He has helped to arrange two international conferences based on which special issues of the academic journal *Rechtstheorie* have been or will be published (entitled 'Rechtspolitik und Gesetzgebung' and 'Multiple Modernität, Globalisierung der Rechtsordnung und Kommunikationsstruktur der Rechtssysteme', respectively). In both cases, the main authors are legal scholars at the University of Tartu. All of this shows that Krawietz has played an outstanding role in giving Estonian legal thought access in global academic fora. Additionally, Krawietz has been a foreign member of the editorial board of *Juridica International*, the law review of the University of Tartu, since the inception of the journal, securing with his participation high academic standards for the publication. He also strongly supported the application of the Estonian Society for Philosophy of Law and Social Philosophy to become a member of the International Society for Philosophy of Law and Social Philosophy (IVR). The application was approved at the world congress of the IVR in New York in 1997.

Taking into account the outstanding scholarly achievements of Professor Werner Krawietz and his contributions to making Estonian legal scholarship more visible in Europe and at a global level, the University of Tartu is very pleased to award him the title of honorary doctor.

Abbreviations

RT	<i>Riigi Teataja</i> (State Gazette)
OJ	Official Journal of the European Union (formerly Official Journal of the European Communities)
CCSCd	decision of the Civil Chamber of the Supreme Court of Estonia
ACSCd	decision of the Administrative Chamber of the Supreme Court of Estonia
CRCSd	decision of the Constitutional Review Chamber of the Supreme Court
ENSV ÜVT	<i>Eesti Nõukogude Sotsialistliku Vabariigi Ülemnõukogu ja Valitsuse Teataja</i> (Gazette of the Supreme Court and Government of the Estonian Soviet Socialist Republic)
ECR	European Court Reports