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Development of Apartment Ownership Legislation in Estonia in 1994–2009 and Reform Plans in the Context of European Judicial Practice

1. Introduction

Apartment ownership represents a construction created by law, which combines the principles of law of property, law of obligations and company law. Particular attention has been paid in legal theory and practice to the legal relationships between apartment owners, i.e., to the internal relationships between owners and the external effects of the relationships. In this paper, I will analyse the development of apartment ownership legislation in Estonia, including the legal nature of the community of apartment owners and its possible development.¹

Since the Apartment Ownership Act² (AOA) is largely based on the Apartment Ownership Act of the Federal Republic of Germany of 1951³ (WEG), I will present a comparative overview of the problems discussed in the local jurisprudence in relation to the community for decades. The German legislator has arrived at the amendment of WEG, by which a community of apartment owners has been given a limited passive legal capacity that was recognised by judicial practice already before. The passive legal capacity of a community of apartment owners has also been recognised in many other legal orders and the AOA also needs to be supplemented.

¹ Apartment ownerships are economically significant in Estonia as out of the 896,000 registered immovables entered in the land register, 461,000 are apartment ownerships (51%). Hence, the percentage of apartments in private ownership is considerably higher than in the Federal Republic of Germany, where the number of apartment ownerships is estimated to be five million. See S. Hügel, O. Elzer. *Das neue WEG-Recht*. München 2007, p. 1.

² Korteriomandiseadus. – RT I 2000, 92, 601; 2006, 43, 326 (in Estonian).

³ Gesetz über das Wohnungseigentum und das Dauerwohnrecht. – BGBl. I pp. 175, 209.

2. Apartment Ownership Acts I and II

The Principles of Ownership Reform Act of 1989⁴ paved way for the privatisation of the dwellings created during the Soviet period. In 1993, the Privatisation of Dwellings Act⁵, was adopted, and pursuant to its § 3, the object of the privatisation was an apartment together with the other relevant part of the dwelling. Here we must say that the reforms went ahead of the development of private law. Civil law did not recognise an apartment that is a physical share of a dwelling as a property law object. Section 14 of the Law of Property Act⁶ (LPA), which entered into force on 1 December 1993, provided that a thing could be in commerce as a whole, as a physical share or as a legal share; yet it did not create an institute of an apartment ownership. The reason is that the LPA was based on the draft Civil Code completed by 1940⁷, which did not recognise the physical share of a dwelling. However, during the privatisation of dwellings, hundreds of thousands of objects similar to apartment ownership entered commerce, whereas dwellings were privatised as separate from the plot underneath then, while later on, the plot was transferred to the owners of the apartments usually free of charge and the apartment ownerships were entered in the register (establishment of apartment ownerships).

The Apartment Ownership Act⁸, based on WEG entered into force on 23 March 1994. Section 1 of the AOA defined apartment ownership as the ownership of an apartment which was a physical share of a structure, and of a legal share corresponding to the size of the physical share of both the plot of land and the essential part of the structure which was not a physical share of any apartment ownership. Such an apartment ownership was regarded as immovable by law, and was subjected to the immovable property provisions of the LPA. Although the AOA was an independent Act, it could be seen as an inseparable but non-codified part of the law of property system.

AOA I did not include provisions governing the maintenance of blocks of flats because of the legal policy decision that the blocks of flats would be maintained through apartment associations as independent legal persons. Administration under a contract of partnership was preserved as an alternative. At the same time, the legislative proceeding of the Apartment Associations Act⁹ (AAA) was in progress in the *Riigikogu* and the Act entered into force on 3 August 1995. It became clear over time that the establishment of apartment associations was not going as planned and a need arose for alternative forms of administration. The situation has been described in the explanatory memorandum to the draft AOA of 2001¹⁰, according to which the need for administering blocks of flats does not depend on whether a separate legal person has been formed, while the duties of an apartment association and its members also remain ambiguous.

AOA II entered into force on 1 July 2001, and continued to define in its § 1 the apartment ownership as ownership of the physical share of a structure together with a legal share of common ownership to which the physical share belongs. The law no longer regards the apartment ownership directly as an immovable; however, according to § 5¹ of the Land Register Act¹¹, an apartment ownership is (registered immovable) entered in the land register as an independent unit. An apartment ownership is a registered immovable from the point of view of formal real right in immovable property, i.e., independent register parts are opened for apartment ownerships in the land register, through which they can be transferred and encumbered. The biggest change included in the AOA was the statutory regulation of the administration of blocks of flats through a community of apartment owners (Chapter 2 'Administration'), which is additionally applied if an apartment association as a legal person has been established to administer the dwelling.¹²

At the moment, the Ministry of Justice has completed the concept of AOA III, which is intended to solve the questions of the passive legal capacity of the community, which have proven problematic, and decide on the possibilities of uniting the apartment association and the community of apartment owners as parallel forms.¹³

⁴ Omandireformi aluste seadus. – RT 1991, 21, 257; 2006, 25, 184 (in Estonian).

⁵ Eluruumide erastamise seadus. – RT I 1993, 23, 411; 2006, 26, 191 (in Estonian).

⁶ Asjaõigusseadus. – RT I 1993, 39, 590; 2008, 59, 330 (in Estonian).

⁷ A. Traat. Tsiviilseadustik (Civil Code). Tartu 1992 (in Estonian).

⁸ Korteriomandiseadus. – RT I 1994, 28, 426 (in Estonian).

⁹ Korterihistuseadus. – RT I 1996, 42, 811; 2006, 61 456 (in Estonian).

¹⁰ Korteriomandiseaduse eelnõu seletuskiri (Explanatory Memorandum to the Apartment Ownership Act). Available at <http://web.riigikogu.ee/ems/saros-bin/mgetdoc?itemid=003671897&login=proof&password=&system=ems&server=ragne11> (10.07.2009) (in Estonian). Explanatory memorandum to AAA: "The presently applicable Act obliges the owners of apartments to establish an apartment association to maintain the shares of apartments in common ownership or to enter into a contract of joint operation. [...] as the apartment association is liable for its liabilities with its assets, the failure to collect the payment from apartment owners or errors in management may quite soon lead to insolvency [...] The situation is absurd from the legal point of view: apartment owners become wealthier on account of the works ordered by the apartment association because the apartment association pays for them and is liable with its assets. The activities of the apartment association are determined by apartment owners who also determine whether the apartment association makes claims to apartment owners."

¹¹ Kinnistusraamatuseadus. – RT I 1994, 94, 1609; 2008, 59, 330 (in Estonian).

¹² AOA § 8 (1).

¹³ Korteriomandiseaduse ja korterihistuseaduse reformi kontseptsioon (Concept of the Apartment Ownership Act and Reform of the Apartment Associations Act). Justiitsministeerium. Tallinn 2008 (in Estonian).

3. Development of community of apartment owners

A community of apartment owners is founded on AOA § 8 (1) which regards as a community of apartment owners their legal relationships concerning the object of common ownership.^{*14} The authors of the AOA of 2001 viewed as a solution to the administration problems in situations where there were no apartment associations as legal persons in most of the blocks of flats the development of legal relationships under the law of obligations between apartment owners:

Since an apartment ownership creates specific obligations and needs arising from the relevant area, which are independent of the existence of legal persons or entry into contracts, to resolve the problematic situation, it would be necessary to establish provisions that determine the legal relationship developed on the basis of law. In the case of a community of apartment owners, it would be a **relationship under the law of obligations** set out in the Apartment Ownership Act and specified by the Law of Property Act, General Part of the Civil Code Act, the Law of Obligations Act after it enters into force, as well as other Acts [author's emphasis – P.P.].

I will examine below how these civil Acts detail the community of apartment owners, i.e., to what extent it can be supported by the provisions of the General Part of the Civil Code Act^{*15} (GPCCA), LPA and the Law of Obligations Act^{*16} (LOA). It is clear that the AOA considers administration based on law as the principal form of administration.^{*17}

The regulation of a community is problematic because there is no clear definition for a community.^{*18} Contrary to the expectations expressed in the explanatory memorandum to the AOA, we can find an unambiguous approach to a community neither in the GPCCA nor LOA. In German law, a community is included in the special part of the law of obligations (BGB^{*19} §§ 741–758). We can find an institute similar to a community in the LOA — a contract of partnership^{*20} (LOA § 580 ff.) — whereas according to Estonian law, a partnership is characterised by achievement of a mutual objective and making contributions thereto, joint management and decision-making, partnership property that is in joint ownership, solidary liability, integrity of partnership property, non-transferability of the rights of a partner, a possibility to terminate and cancel a partnership. According to § 2 (2) of the Non-profit Associations Act^{*21} (NAA), associations of persons with non-profit characteristics which are not entered in the register are not legal persons and the provisions for civil law partnerships apply to them. Spouses and co-successors also serve as a community.^{*22}

However, a community was still regarded in LPA § 70 (7) (shared ownership), published in 1999, which precludes the application of provisions of a partnership. Namely, the provision sets out that if a right belongs to several persons (community), the provisions concerning joint ownership are applied thereto unless otherwise provided by law. This section appeared in the draft Law of Property Act, Law of Property Act Implementation Act, Land Register Act and Code of Enforcement Procedure Amendment Act^{*23} on the initiative of its initiator (Ministry

¹⁴ AOA § 8 (1): “On the basis of an agreement, apartment owners may organise legal relationships concerning the object of common ownership (community of apartment owners) differently than provided by this Act, except if this is directly precluded by law. If apartment owners decide to found an apartment association pursuant to the requirements of the Apartment Associations Act, the owners shall administer the object of common ownership pursuant to the Apartment Associations Act as of the creation of the legal capacity of the apartment association. In the case provided for in the previous sentence, this Act applies to administration of the object of common ownership in so far as this is not in conflict with the Apartment Associations Act.”

¹⁵ Tsiivilseadustiku üldosa seadus. – RT I 2002, 35, 216; 2008, 59, 330 (in Estonian).

¹⁶ Völaõigusseadus. – RT I 2001, 81, 487; 2008, 59, 330 (in Estonian).

¹⁷ Explanatory memorandum to the AOA (Note 10): “The draft Act mostly proceeds from the German Apartment Ownership Act and judicial practice. The structure of the Estonian Apartment Ownership Act has remained the same; provisions concerning administration have been added along with procedural provisions required by the administration provisions. [...] According to the draft Act, an apartment association will remain included in our law as an alternative to a community of apartment owners. The draft Act abolishes the requirement for an obligatory apartment association. [...] The draft Act does not limit in any manner the activities of the existing apartment associations or the foundation of new apartment associations.”

¹⁸ Kaupo Paal has regarded aspects related to a community of apartment owners in his article “Völaõigusseaduse mõju valitseja nimetamisele ja õigusastele korteriomaniikega” (Impact of the Law of Obligations Act on Appointment of Administrator and Legal Relationships with Apartment Owners) (Juridica 2003/5) (in Estonian) and the passive legal capacity of a community of subjects who are not legal persons has been discussed in the doctoral thesis of Kalev Saar “Eraõigusliku juriidilise isiku õigussubjektuse piiritlemine” (Delimitation of the Subject of Law Status of a Legal Person Governed by Private Law), published by TÜ Kirjastus under the same title in 2004 (in Estonian).

¹⁹ BGBI. I 42 p. 2909; 2003 I p. 738.

²⁰ Note 17.

²¹ Mittetulundusühingute seadus. – RT I 1996, 42, 811; 2008, 59, 330 (in Estonian).

²² A community must be regarded as a community of persons, just as spouses; in both cases, a community owns property in undivided parts (joint ownership). See K. Saare. Eraõigusliku juriidilise isiku õigussubjektuse piiritlemine (Delimitation of the Subject of Law Status of a Legal Person Governed by Private Law). Tartu 2004, p. 78 (in Estonian).

²³ Asjaõigusseaduse, asjaõigusseaduse rakendamise seaduse, kinnistusraamatuseaduse ja täitemenetluse seadustiku muutmise seadus. – RT I 1999, 27, 380 (in Estonian).

of Justice) before the adoption of the draft, which is why the explanatory memorandum to the draft does not contain the reasons of the amendment. Hence, the general notion of a community has been defined via the law of property or application of the provisions regarding (joint) ownership. If a thing belongs to several persons, it is presumed that a common ownership exists; if a right belongs to several persons, we can presume that the right belongs to the persons in legal shares and we proceed from the rules of common ownership when exercising the rights and obligations relating to legal shares.^{*24} According to the explanatory memorandum to AOA, the joint exercise of rights must be regarded as a law of obligations, not a property law relationship. It is also evident from the second chapter of the AOA that besides the provisions of common ownership special provisions arising from the AOA or agreements of apartment owners (so-called right to exercise will) must be applied.^{*25} Because of the detailed nature of the AOA, it is applied above all and the LPA only applies to individual areas for which there are no special provisions in the AOA. Thus, for example, based on LOA § 79 (2), any agreements between co-owners concerning the procedure for use of a shared thing are entered in the land register.

It is obvious that the notions of community provided in LOA § 70 (7) and AOA § 8 (1) do not coincide. While LPA § 70 regards as a community the joint ownership of rights, AOA § 8 (1) regards as a community of apartment owners the legal relationships concerning the object of common ownership, i.e., the mutual rights and obligations as well as the rights and obligations to third parties. The wording of WEG § 10 (2) can be considered more appropriate as it sets out that the provisions of community of the BGB are applied to the relationships between apartment owners because it does not derive otherwise from the Apartment Ownership Act.^{*26}

4. Nature of community of apartment owners

When defining the community of apartment owners, regard must be given besides the law of obligations to the relationships of the institute with company law since directing bodies are connected with the administration of apartment associations, which serves as a feature of associations and not of joint ownership.^{*27} As a community has arrived in Estonian law via the impact of German law, I will present a comparative overview of defining a community of apartment owners.

When defining a community of apartment owners, we also have to define the nature of an apartment ownership. This is complicated by the fact that an apartment ownership consists of various elements (plot, apartment, the administrative property of apartment owners, apartment owners' rights to vote, etc.), which gives rise to the question what the object in commerce is in the case of an apartment ownership.^{*28}

WEG § 1 regards the special ownership (physical ownership)^{*29} and the share in the common ownership as a single legal entity (*rechtliche Einheit*)^{*30}, in which the share in the common ownership is necessary in order to enter the apartment ownership in the land register (in the case of an apartment ownership, special ownership is in the foreground and common ownership is its accessory).^{*31} The prevailing German approach admits here that several corporate elements relate to the shared ownership and special ownership. The theory divides apartment ownership into three parts: besides the special ownership and the share in the common ownership there is also the membership element, i.e., the right and obligations arising from the community of apartment owners.^{*32}

Hence, the apartment ownership by nature belongs to the mixed legal type consisting of law of property and law of obligations elements. None of the elements stand out among others. Because of the uniformity of the elements, the rights arising from the membership of the community also transfer to the transferee upon the transfer of the apartment ownership. An apartment ownership is a unique legal institute, an original ownership that can be

²⁴ Pursuant to § 147 of the Law of Succession Act that entered into force on 1.01.2009, if several successors have accepted the succession (co-successors), the estate is owned by the successors jointly (community of the estate), to which the provisions of common ownership apply. A co-successor may not dispose independently of the items that belong to the estate, but may dispose of the legal share in the community of the estate. – RT I 2008, 7, 52 (in Estonian).

²⁵ AOA § 8 (2)–(4).

²⁶ Palandt. Bürgerliches Gesetzbuch. Kommentar. 67. Aufl. München 2008, § 741, p. 1102.

²⁷ In German legal theory, the theory of association of apartment ownerships has remained isolated so far, yet there are several overlaps between the possibility of establishing an apartment association based on the AOA and the German theory of associations. K. Paal. Korteriomandiseaduse väljatöötamise alustest (On the Foundations of Preparing the Apartment Ownership Act). – Juridica 2001/4, p. 274 (in Estonian).

²⁸ A. Brehm. Sachenrecht. Mohr Siebek Verlag 2006, p. 380.

²⁹ Wesenberg admits that an apartment ownership as an ownership defined in the Apartment Ownership Act is a special ownership in two ways — it includes special ownership and serves itself as special ownership. See A. Brehm (Note 28), p. 12.

³⁰ J. Bährmann. Wohnungseigentum. München 1991, p. 9.

³¹ In comparison, according to judgment No. 3-2-1-164-05 of the Supreme Court of Estonia of 11.04.2006, in the case of an apartment ownership created as a result of privatisation, it is the special ownership (apartment) that is in the foreground, so an apartment serving as the separate property of spouses does not become the joint property of spouses even if an apartment ownership is established, if this happens during the marriage.

³² E. Pick. Wohnungseigentumsgesetz. München 2007, p. 39.

furnished with a content because the content of the apartment ownership could be developed by the agreement of apartment owners to the extent not prohibited by law (*typus sui generis*). AOA § 8 (2–4) generally allow for free development of the membership rights serving as the content of apartment ownership. This applies to a special legal successor insofar as the agreements differing from law have been entered in the land register.

A particular association of people is created upon the establishment of apartment ownerships. The membership of the association, above all, relates to law of property. A share in the common ownership is an integral part of special ownership, while there is also an indirect link between a share in common ownership and a share held by each member of the community in the assets of the community. AOA § 1 (2) defines the object of common ownership so that a plot of land and such parts of a structure which are not in sole ownership are in the common ownership of apartment owners. This gives rise to the question in Estonian legal order about the ownership of the assets accumulated collectively. The assets of a community are made up of the acts of apartment owners that they are obliged to perform in line with the size of their share in the common ownership, but it also encompasses obligations, movable property required for administration, receivables from other apartment owners and third parties, as well as the fruit from shared ownership, etc. The assets of a community do not belong to the common ownership related to special ownership but it belongs to the community — the membership of the community entails the right to receive part of these assets. In essence, each apartment owner holds an independent legal share of the assets of the community, yet it cannot be disposed of independently or pledged without the apartment ownership. The claims of the community do not constitute a common obligation relationship in which case all the apartment owners could demand its satisfaction.³³ A claim must be satisfied to the community as such.

AOA §§ 1 and 8 do not contain an immediate reference to the provisions of common ownership, yet § 1 sets out that the provisions of the Law of Property Act concerning immovable property ownership apply to apartment ownership in issues not regulated by the Act (which precludes the application of the provisions of the LOA concerning a partnership). The German theory criticises the application of the BGB (§ 741) provisions on community as the provisions of the law of obligations to an apartment ownership because in reality their application is of little significance. Because of the directing bodies, Brehm finds that a community of apartment owners is organised in the same way as a legal person.³⁴ Some authors regard a community related to the apartment ownership rather as a partnership in which undivided joint property is created for the participants.³⁵ The use of a partnership would be difficult because the owners need not be bound by personal trust and confidence. The difference between a partnership and a community is that a partner cannot dispose of a legal share of the partnership property³⁶, whereas such a right of disposal is held by the members of a community (disposal still requires an apartment ownership). A community of apartment owners is a community of rights that have legal shares, which means that the size of the share each member has in the community is predetermined. While a partnership is usually created based on an agreement, a community is established by law.

All in all, a community of apartment owners formed pursuant to Estonian law is a community *typus sui generis*, the existence of which requires the following preconditions: an apartment ownership cannot exist without a community; a community is created based on law; a community functions through the Apartment Ownership Act or the expression of will permitted by law; only apartment owners can be members of a community (obligatory membership); unlike in the case of common ownership, an apartment owner cannot terminate a community (AOA § 9), neither can the apartment owner transfer or pledge it as parts separate from the apartment ownership. Here we must also point out the organisational structure of a community (the existence of a general meeting, house council, administrator, AOA §§ 17, 20 and 23).³⁷ If all the apartment ownerships belong to the same person, he or she cannot serve as a community of a single individual.

5. Passive legal capacity of a community of apartment owners

The existence of independent liability, as well as the ability to take on rights and obligations, is decisive in the case of a community of apartment owners. The prevailing approach in German legal theory had not recognised the passive legal capacity of a community of apartment owners until 2005. However, attempts were made in relation to a community of apartment owners to find similarities with other communities of persons who did

³³ I. Kull, M. Käerdi, V. Kõve. *Võlaõigus I. Üldosa* (Law of Obligations I. General Part). Tallinn 2004, p. 419 (in Estonian).

³⁴ A. Brehm (Note 28), p. 380.

³⁵ M. Lutter. *Theorie der Mitgliedschaft*. AcP 1980, Volume 180, paragraph 146; J. Bährmann (Note 30), p. 114. Yet such associations constitute communities oriented to a particular goal (*Zweckgemeinschaft*), while in the case of apartment owners a community is rather oriented to exercising common interests (*Interessengemeinschaft*).

³⁶ P. Varul, I. Kull, V. Kõve, M. Käerdi. *Võlaõigusseadus II. Kommenteeritud väljaanne* (Law of Obligations Act II. Commented edition). Tallinn 2007, p. 671 (in Estonian).

³⁷ Unlike in the partnership and common ownership. The bodies of a community of apartment owners can also be external bodies in the form of an administrator appointed from outside. S. Renner. *Die Wohnungseigentümergeinschaft im Rechtsverkehr*. Berlin 2005, p. 41.

not have passive legal capacity, above all, with partnerships.^{*38} Estonian law also recognises associations of persons that are not legal persons to which provisions of civil law partnerships are applied (NAA § 2 (2)). K. Saare has been of the opinion that because of the organisation, identity and liability assets of a partnership, the recognition of the passive legal capacity of a partnership would be justified for practical reasons.^{*39} The same practical reasons apply to a community of apartment owners. If an administrator enters into an agreement for purchasing a service, the administrator would do it in the name of the community, not apartment owners, i.e., the party to the agreement is the community.

The liability of apartment owners for the performance of the agreement is unclear in Estonian law and criticism towards limiting the liability of apartment owners may be justified because a community and also an apartment association often lack enough assets to be liable. Problems of liability arise also if any of the members of the community are replaced. Whereas a new partner in a partnership is expected to be liable for the earlier obligations only by a special agreement with the creditor, the prevailing opinion is that a new apartment owner is also liable for the obligations of the former owner in a community of apartment owners. The reason is that the community is of an obligatory nature in which the rights and obligations arising from membership are inseparably related to the special ownership and share in the common ownership. In Estonian law, the transfer of obligations to the transferee has not been directly set out in the AOA but the principle has been set out in AAA § 7 (3). At the same time, the judicial practice of the Supreme Court has denied the automatic transfer of the former owner's obligations to the new owner and regarded such obligations as personal obligations.^{*40}

Since the AOA is based on the WEG, it is important to discuss the amendments made to the WEG in 2007^{*41}, which sum up as positive law the previous discussion and the judicial practice of higher courts in recognising the passive legal capacity of a community.^{*42} Subsection § 10 (1) of the Act sets out a general rule that apartment owners bear the rights and obligations arising from an apartment ownership but the provision also provides for a possibility to set out differently by law. According to supplemented subsections 6–8, a community of apartment owners may, within the framework of administering a shared ownership, assume rights and obligations both to third parties and apartment owners themselves. A community may file an action and be actionable.^{*43} A community is recognised as a subject of law, yet it is not considered a legal person.^{*44}

WEG § 10 (7) also sets out the ability of a community to own assets necessary for administration, consisting of things acquired during administration, including money, rights and obligations, as well as claims against third parties and apartment owners. A community may acquire real rights in immovable property only within the framework of common administration.^{*45}

WEG § 10 (8) adds provisions concerning the liability of apartment owners to a community of apartment owners. Each apartment owner is liable to the creditor for the performance of the obligations of the community in proportion to his or her share in the common ownership, if the obligations have arisen or become recoverable during the period when the apartment owner was a member of the community. It is limited partial liability.^{*46} An apartment owner is liable to the community for the performance of his or her obligations based on the legal share of common ownership. It is not, however, additional liability, but a creditor is able to file a claim directly against the owner.^{*47} WEG § 11 allows for declaring a bankruptcy regarding the assets of the community, which in itself does not entail the termination of the community.^{*48} It is possible to apply § 93 of the German Bankruptcy Act, according to which a trustee in bankruptcy may make a claim for payment against the members of the community.

³⁸ A decision of BGH dated 29.01.2001 was decisive, defining a partnership as having passive legal capacity and procedural capacity. – ZIP 2001, p. 330.

³⁹ K. Saare. *Seltsing – kas leping või ühing? (Partnership — Agreement or Association?)* – *Juridica* 2003/1, p. 64 (in Estonian).

⁴⁰ In the judgment of Supreme Court in civil matter No. 3-2-1-105-05, 2.11.2005 (RT III 2005, 38, 371), the Court has established that the debts not paid by the former owner do not transfer to the new owner unless separately agreed upon. The judgment also assumes a position that the obligations created from the moment of becoming the owner must be borne by the new owner in relations with the other co-owners. Each co-owner is liable for the performance of the obligations that have become recoverable during the period when he or she has been a co-owner.

⁴¹ BGBl. I p. 2866.

⁴² In 2005, the Supreme Court of the Federal Republic of Germany (BGH) recognised the partial passive legal capacity of a community of apartment owners **insofar as it participated in the administration of shared ownership in legal proceedings**. According to that, a community of apartment owners may have rights and obligations, serve as a respondent and plaintiff and participate in an execution proceeding as a debtor and a creditor. Pursuant to the judgment concerned, a community of apartment owners cannot file claims against a member of the community and in this case apartment owners have the right of claim because such a claim does not involve 'participation in commerce'; however, a community can file such claims against third parties.

⁴³ Apartment owners may file an action against a community and a community may file an action against apartment owners.

⁴⁴ L. Rühlcke. *Gesamthand, rechtsfähige Personengesellschaft, juristische Person und Wohnungseigentümergeinschaft*. – *Zeitschrift für Wohnungseigentumsrecht (ZWE)* 2007 (8) 7, p. 266.

⁴⁵ J. Demharter. *Grundbuchordnung*. 26. Aufl. München 2007, p. 332.

⁴⁶ W. Boeckh. *Wohnungseigentumsrecht*. Baden-Baden 2007, p. 60.

⁴⁷ G. Jennissen. *Wohnungseigentumsgesetz*. Köln 2008, p. 166.

⁴⁸ E. Braun. *Insolvenzordnung*. 3. Aufl. München 2007, p. 118.

In addition, the rights and obligations of an administrator of an apartment ownership to the community have been specified in WEG § 27. An administrator is regarded as a directing and representative body of a community that has passive legal capacity. If there is no administrator, apartment owners represent the community jointly, unless the right of representation has been transferred to one or several apartment owners by a resolution of the apartment owners.

Several European legal orders have recognised the limited passive legal capacity of a community of apartment owners; some countries have even recognised the concept of an independent legal person.^{*49}

According to the Swiss Apartment Ownership Act of 1965, which proceeds from a specially developed concept of common ownership, a community of co-owners has a limited legal capacity and the community may independently assume obligations, own assets necessary for its activities, file actions and be actionable, and is represented by an administrator. The concept of liability departs from the precondition that each apartment owner is liable for the obligations of the community to the extent of the legal share owned by him or her, i.e., not solidarily.^{*50}

According to the French Apartment Ownership Act of 1965, a community of apartment owners (*syndicat*) is created by law and has passive legal capacity.^{*51}

Section 2 of the Austrian Apartment Ownership Act of 2002 regards an apartment ownership as a real right and a community of apartment owners *expressis verbis* as a legal person having limited passive legal capacity, represented by an administrator. According to § 18 of the Act, a community may assume obligations and rights in administration as well as serve as a plaintiff and defendant. As regards the concept of liability, additional liability is presumed based on the size of the legal share of the common ownership of the apartment owner if an execution proceeding from the assets of the community is not a success.^{*52}

Pursuant to § 124 of the new Dutch Civil Code, a society of owners (*vereniging van eigenaars*) holding apartment rights (*appartementsrechten*) created as a result of dividing an immovable is a legal person, while all the apartment owners are obliged to be its members.^{*53}

6. Interrelationship between community of apartment owners and apartment association

The explanatory memorandum to the AOA viewed an apartment association merely as an alternative to a community, not a rule. An apartment association is a legal personality that has been formed for the administration of blocks of flats, i.e., the formation of the association and the election of its management board substitutes for the appointment of the administrator for the purposes of the AOA. According to § 2 of the Act, the association is a non-profit association that is besides the AAA also subject to the NAA and is entered in the non-profit associations register maintained by the court.^{*54} Just as in the case of a community, membership of the apartment association is obligatory (AAA § 5 (1)) and although a separate memorandum of association is not entered into, an apartment association is not created automatically upon the establishment of apartment ownerships. Pursuant to AAA § 6, an apartment association has independent assets, apartment owners are liable for the obligations assumed by the association only to the extent of the contributions made, which limits the liability of apartment owners, although it is usually the apartment owners who gather wealth on account of the expenses incurred by the association.^{*55} Apartment owners are not liable to the creditors of the association but the claims of the association against its members are secured by a mortgage established in the apartment ownerships.^{*56}

⁴⁹ The lack of passive legal capacity has been regarded as a negative factor in making investments in the housing sector. See R. Fritsch. *Das neue Wohnungseigentumrecht*. Baden-Baden 2007, p. 18.

⁵⁰ T. P. Ruetschi. *Das schweizerische Stockwerkeigentum*. Zürich 1980, pp. 31, 36.

⁵¹ S. M. Wietek. *Wohnungseigentum in Frankreich*. Frankfurt 1976, p. 72.

⁵² B. Schober. *Rechte und Pflichten der Eigentümergemeinschaft*. Wien 2004, pp. 23, 45.

⁵³ A. S. Westerdijk. *Niederländisches Bürgerliches Gesetzbuch*. Buch 5 Sachenrecht. München 1996, p. 291.

⁵⁴ AAA § 2 (1): “An apartment association is a non-profit association established by apartment owners provided for in the Apartment Ownership Act [...] for the purpose of shared management of the legal shares of the buildings and plot of land which are part of the object of apartment ownership and representation of the shared interests of the members of the apartment association.”

⁵⁵ According to judgment No. 3-2-1-111-04 of the Supreme Court dated 30.11.2004, an apartment association is, based on AAA § 2 (1), a representative of the interests of apartment owners; hence, an apartment association may enter into a subscription contract and a sales contract of heat with a network operator. If an apartment association enters into a sales contract of heat on behalf of itself, it is also liable to the network operator for the performance of the contract. Thus, the apartment association distributes heat between apartment owners and claims from the apartment owners their proportional part of the management expenditure according to the resolutions of the apartment association and its articles of association. – RT III 2004, 36, 373 (in Estonian).

⁵⁶ AAA § 9 (1). The Act does not specify whether the mortgage arises from law or the association has a right of claim for the establishment of the mortgage.

Consequently, an apartment association and a community of apartment owners have a number of similarities in the Estonian legal order, while the greatest difference is that the association has a passive legal capacity and assets. Pursuant to AOA § 8 (1), the provisions of the AOA apply also to administration of the object of common ownership when an apartment association has been formed in so far as this is not in conflict with the AAA. Difficulties in interpreting the nature of the apartment association result from a legal maze, in which the NAA and AOA must be applied to the activities of the association besides AAA. It is incomprehensible why the actual solutions of the administration of blocks of flats must be different in a community and association. This gives rise to the need to harmonise the provisions of the AAA and AOA or once the judicial practice recognises the passive legal capacity of a community of apartment owners, there would be no need for an apartment association as a legal person.

7. Concept of Apartment Ownership Act III

7.1. Choices between different forms of administration

The Concept of the Reform of the Apartment Ownership Act and Apartment Associations Act^{*57}, which offers unique solutions considering the regulations adopted in Europe in setting out the passive legal capacity of the community, prepared in the Ministry of Justice, seeks solutions for the problems described in the previous sections.

There are three ways of regulating the administration of apartment ownerships:

- 1) to preserve the present dualism between the community and apartment ownership;
- 2) a community that is not a legal person but the passive legal capacity of which has been strengthened will be the only form of administration;
- 3) an association that is a legal person will be the only form of administration.

Version 1 involves a contradiction that the unjustified dualism will preserve, three different Acts (AOA, AAA, NAA) are applied, it is difficult to understand a community in legal proceedings. The advantages of maintaining the present system would be the continuing legal peace, i.e., nobody is compelled to change the form of administration and different forms allow for flexible consideration of the needs of blocks of flats of various sizes.

Version 2 is contradicted by the fact that the present communities should be liquidated and this would not be met with approval in legal proceedings; the advantage would be that the administration of blocks of flats would be organised on the same bases with the system prevailing in Continental Europe, which would match up better with our civil law.

Version 3 would have the advantage of preserving the present apartment associations that have been adopted more readily than the communities of individuals that are not legal persons. A status of a legal person has been analogously granted to a general partnership in our legal order (§ 79 of the Commercial Code).^{*58} Such an association would serve as a compulsory association or a legal person *typus sui generis*. The disadvantages are that a legal person would also be created where it would not be necessary (small houses), while additional (financial) obligations (such as independent accounting) ensue from a legal person. If in a community an apartment owner serves as a client through a general meeting and the administrator engages in administration, then in an association a greater liability and a more active role in administering the house is expected from apartment owners, for which they need not be prepared. Administration through a compulsory legal person would set a precedent in Europe, which is why its relations with the rest of civil law must be carefully considered.

The legislator, in essence, has two solutions: to recognise the limited passive legal capacity of a community of apartment owners and dissolve apartment associations or to create by law a situation in which it is compulsory to form an apartment association upon the establishment of apartment ownerships or to provide that an apartment association as a legal person is created automatically, so it will not be necessary to regulate the passive legal capacity of a community as a personal society. Since there are approximately 9000 apartment associations in Estonia, according to the information system of the commercial register, their liquidation would be an extremist choice with regard to legal traditions. It would be easier to regard communities as legal persons created on the basis of law (apartment associations) based on the examples set by the Netherlands and Austria.

The completed concept prefers version 3 and it should be accepted regardless of its flaws.^{*59} First of all, it is necessary to determine how such a legal person would be created. Section 26 of the GPCCA presumes

⁵⁷ Note 13.

⁵⁸ Äriseadustik. – RT I 1995, 26–28, 355; 2009, 12, 71 (in Estonian).

⁵⁹ Concept (Note 13), p. 12.

the creation of passive legal capacity through making an entry in a register (without specifying the register). According to the present regulation, an apartment association is created by making an entry in the register of non-profit associations.⁶⁰ An alternative would be to enter an apartment association in the land register — it would be necessary to establish a general part or a separate box in the register part of apartment ownership (the administrators of state assets are entered in the land register in the same way). The general part would contain the general data on the registered immovable and there would be no need to repeat them in individual register parts. A disadvantage of the alternative is that it would require considerable reorganisation of the land register law and the register itself, also giving rise to the question whether the existing associations should be reregistered.

It would be less painful to continue with a system in which the present associations and future obligatory associations would be entered in the register of non-profit associations, which would, above all, eliminate the need for reregistering the associations. There is still a disadvantage that both the land register and the register of non-profit associations would have to be examined in legal proceedings; however, the problem can be solved by provision of online access. If an association remains the only form of administration, it is an obligatory association; hence, such an association must be created along with opening the register parts of apartment ownerships. The concept suggests that the registrar open a registry card for an association and the register of non-profit associations tackle the legal issues from that point onwards.⁶¹ Such a procedure is acceptable because it is necessary to contact the register of associations to identify the right of representation of an owner who is a legal person in real property transactions today. The title page of the land register should still show the name and registry code of the association.

7.2. Specifications related to company law

The next step is to answer the question how an apartment association should be defined in company law and to what company type it bears the closest resemblance, i.e., whether the Non-profit Associations Act should continue to be applied, or the association is a commercial association aimed at joint activities, to which the Commercial Associations Act should be applied⁶², or it is an independent type of company to which only the general part of the GPCCA is applied. When analysing the objectives of the activities of an apartment association, they are clearly oriented to commercial activities. Although an apartment association does not pay dividends, the association still serves the economic interests of its members and presumes the joint activities of its members like a commercial association. Unlike a commercial association and a non-profit association, an association cannot control its members because the membership comes with an apartment ownership. Due to lack of attachment of the members, an apartment association is sooner similar to a public limited company. The concept offers to create a completely independent regulation for an apartment association in the AOA and to supplement GPCCA § 25 with a new type of a legal person, which eliminates problems related to the application of several Acts.⁶³ It is hard to agree to this since it is rather characteristic of a legal order to apply the rules of a body subsidiarily similar to a special type of an association (political parties, congregations, etc.). It would not be justified to apply regulation different from that applied, for example, to housing associations which are entered in the register of non-profit associations and to which the provisions of commercial associations are additionally applied.⁶⁴

Basic data are required when the foundation of an apartment association is registered by an assistant judge opening the register parts of apartment ownerships. This gives rise to the question whether a memorandum of association and the articles of association are necessary. It would be logical if the memorandum of association is contained in the application to divide an immovable into apartment ownerships and no separate memorandum of association is entered into.⁶⁵ AAA § 3 (1) provides today that a memorandum of association is not entered into upon the foundation of an apartment association. A legal person in private law has articles of association or a partnership agreement according to GPCCA § 28. A present-day apartment association is required to have articles of association as well. The concept does not presume that an apartment association has articles of association at all times, especially in the case of smaller associations in which the regulation of the Act is sufficient.⁶⁶ When proceeding from § 15 (6) of the applicable AOA, it is expected that apartment owners establish internal rules that are by nature analogous to the articles of association. In an obligatory

⁶⁰ NAA § 3.

⁶¹ Concept (Note 13), p. 14.

⁶² Tulundusühistuseadus. – RT I 2002, 3, 6 (in Estonian).

⁶³ Concept (Note 13), p. 16.

⁶⁴ Subsection 1 (2) of the Dwelling Associations Act (hooneühistuseadus). – RT I 2004, 53, 368 (in Estonian).

⁶⁵ Junkers in his theory of associations regards a community of apartment owners as an independent law of property society (*dingliche Gesellschaft*), in which an agreement between apartment owners for the establishment of apartment ownerships also represents a partnership agreement. M. Junkers. Die Gesellschaft nach dem Wohnungseigentumsgesetz. München 1993, p. 281 ff.

⁶⁶ Concept (Note 13), p. 17.

association, it should be taken as the basis that an association has articles of association that substitute for the internal rules and all the amendments to the articles of association (internal rules) can be seen from the register. This would eliminate the need to enter any agreements derogating from law as specified in AOA § 8 (2) in the land register. It has to be decided whether an agreement on the procedure for the possession and use of the shared ownership (plot, basement, etc.) of blocks of flats could be governed by the articles of association or whether it should be entered in the land register as an issue regarding the law of property. The concept suggests that such issues be regulated by the articles of association^{*67}, but in such a case, it is difficult to ensure the protection of the rights of third parties (an amendment to the procedure for use of common ownership, for example, relates to the interests of a mortgagee and the ranking of the entry concerning procedure for use is important in an execution proceeding).

The objective of the new regulation must be to harmonise the mechanism of making decisions. AOA § 12 presumes that the resolutions of apartment owners are reached by consensus and only issues regarding normal use are decided by majority vote. Such a provision differs both from LPA § 72 (1), according to which co-owners may decide on the possession and use of a thing by a decision of the majority and an apartment association in which issues regarding administration can be adopted by majority vote. The provisions must ensure that the present situation, in which the same persons start a general meeting to decide on law of property issues after a general meeting of an apartment association has ended, is discontinued. A distinction must be made regarding which decisions can be reached by consensus and which by majority vote. The number of the votes of apartment owners must also be harmonised. According to AAA § 11, each apartment owner has one vote, i.e., each apartment ownership gives one vote. AOA § 19 gives an apartment owner one vote regardless of the number of apartment ownerships in order to avoid excessive influence of one person. In the case of common ownership, LPA § 72 proceeds from the size of the ownership. It seems more appropriate to retain the solution contained in the AAA, in which one apartment ownership gives one vote at a general meeting.

When introducing an obligatory apartment association, the present triple administration form — general meeting (AOA § 17), administrator (AOA § 20), house council (AOA § 23) — in which the administrator is a representative body of the community acting under an authorisation agreement must be abandoned. In an association, a management board serves as a representative body, which presumes that there are enough apartment owners capable of administration in the house but the members of the management board may also come from outside the circle of owners. Lack of apartment owners competent in housing may prove a problem, which is the reason why the administration service is partly outsourced, as evident in the present associations. The concept suggests that a management board need not be elected in smaller associations and apartment owners jointly have a right of representation.^{*68} Assuming that there may not be people with sufficient experience and time resources in the apartment association to organise everyday administration, it should be considered to retain the administrator (as the administrative body of a community) and regulate the internal relations between the administrator (as a procurator) and the association (management board).

7.3. Apartment owner's liability for association and to association

The applicable law does not rule out the insolvency of an apartment association and the commencement of bankruptcy proceedings, while apartment owners are liable to the association and not to the creditors of the association. Apartment owners are liable in a community that does not have passive legal capacity. In an obligatory association, the membership is related to ownership, so it is essentially impossible to liquidate an association on the grounds of insolvency^{*69}, and the new regulation must provide for the supplementary liability of apartment owners also upon the formation of a legal person.

It would be appropriate to analogously apply the regulation of a general partnership where according to § 101 of the Commercial Code, the solidary liability of the partners applies to all the obligations of the partnership, which can, however, be enforced only after the creditor failed to receive full satisfaction of his or her claims from the assets of the partnership. WEG § 10 (8) sets out the partial liability of apartment owners for the obligations of the community, depending on the size of the legal share of common ownership, but a creditor may file a claim jointly against both the community and apartment owner. As an apartment association is a specific commercial association, acting in the field of housing, it would be justified to apply the principle of subsidiary partial liability, in which case a creditor may file a claim not satisfied by the association against the apartment owner depending on the size of his or her common ownership.^{*70}

⁶⁷ *Ibid.*

⁶⁸ *Ibid.*, p. 19.

⁶⁹ WEG § 11 (3) precludes commencement of bankruptcy proceedings against the assets of a community.

⁷⁰ Concept (Note 13), p. 34.

The liability of the transferee of an apartment ownership for the debts incurred by the previous owner should be further specified. AAA § 7 (3) provides that the new owner is liable for all the unpaid obligations of the previous owner. Such a simplified approach needs to be differentiated since both the continuation of the liability of the previous owner and the new owner's liability for obligations assumed by the previous owner, which have become recoverable after the transfer of the ownership, need to be settled (e.g., loans for major repairs). The regulation of general partnership should be taken as an example as according to § 102 of the Commercial Code, a former partner of the general partnership is also solidarily liable with the other partners within five years.^{*71} Such a liability must be related to the obligations assumed during the period when the former apartment owner was the owner. The liability of the new owner for the unpaid obligations of the former owner also needs to be limited and could be limited to the value of the apartment ownership or the apartment ownership itself, not to the personal property of the new owner.^{*72}

8. Conclusions

The law of property content of the institute of apartment ownership in Estonia has been developed similarly to the German WEG, in which an apartment ownership consists of a physical share and a legal share of a common ownership in the registered immovable which is an integral part thereof. The legal relationships created between apartment owners need to be reformed in order to eliminate ambiguity regarding the extent of the liability of the apartment owners and different legal treatment in dwellings for the administration of which an apartment association has been established and in dwellings where there is no apartment association. A community of apartment owners established on the basis of the AOA has the following characteristics: an apartment ownership cannot exist without a community developing on the basis of law; the community functions through the rules of the APA or the expression of will of the apartment owners as permitted by law; only apartment owners can be members of the community of apartment owners (obligatory membership). A community of apartment owners is described by the organisational structure of the community or the existence of directing bodies (general meeting, house council, administrator). An important feature distinguishing between a community of apartment owners and common ownership (as well as partnership) is the fact that nobody can demand the termination of the community. Due to certain similarity, the application of provisions concerning a partnership to a community could be considered since the explanatory memorandum to the AOA regards a community as based on a law of obligations relationship. NAA § 2 also implies the possibility of applying the provisions concerning a partnership, by prescribing the application of partnership provisions to a non-profit association of persons that is not a legal person. At the same time, the AOA refers to the application of provisions concerning immovable property ownership and hence the provisions of common ownership. Most of the time, the provisions of common ownership are not applicable since the AOA contains enough special provisions. A community of apartment owners does not, in fact, coincide with any association of persons, so according to the Estonian law it is a community *typus sui generis*. Such a new type of personal association has not been discussed in legal theory and judicial practice, which is why the issues of the passive legal capacity and independent assets of a community have not been settled. The topic is important in the context in which an apartment association has such passive legal capacity and independent assets, while administration has been organised differently.

When examining the amendments made to the WEG in 2007, as well as the civil laws of the Netherlands, Switzerland, Austria and France, a legal personality has been granted to a community to meet the needs of legal proceedings. Legal personality is characteristic of individuals. According to German law, a community is a subject that has passive legal capacity created by law, which does not need to be entered in the register to be created. Granting passive legal capacity created under law to a community of apartment owners also in Estonia gives rise to the question why distinguish between a community and association as two forms of administration that have similar objectives. When recognising the passive legal capacity of a community by law, starting from the establishment of apartment ownerships and delimiting the liability of the members of a community for the obligations of a community, there is no need for the foundation of an apartment association as a separate legal person. It has to be admitted that the implementation of such a change would be difficult because of the large number of apartment associations, which is why it would be reasonable to regard the passive legal capacity of an apartment association as created by the formation of apartment ownerships by law, while the registrar of the land register *ex officio* makes relevant entries in the non-profit associations register.

⁷¹ WEG § 10 (8) also sets out the five-year solidary liability of the former owner.

⁷² Concept (Note 13), p. 35.