AMENDMENTS TO POLISH COMPANIES LAW – UPDATED DRAFT BILL

On 17 August 2021, the Polish Council of Ministers approved the updated draft of the bill to amend the Commercial Companies Code ("CCC") and certain other acts. The draft bill was then submitted to the Polish Parliament on 23 August 2021.

Compared with the draft published half a year ago, the August 2021 draft does not introduce significant changes.

The primary purpose of the bill is to introduce into Polish law novel legal regulations in respect of holdings and moreover a range of amendments strengthening the position of supervisory boards, by providing them the tools needed to more effectively exercise corporate supervision.

We present the most important provisions of the draft amendments below.

HOLDING LAW

> Corporate groups

The draft amendments allow existing holdings, i.e., structures consisting of companies related to each other based on dominant and subsidiary relationships, including de facto holdings, to collectively do business within a newly proposed legal framework for, so-called, corporate groups.

According to the proposed definition, a corporate group consists of **a parent company and its subsidiary or subsidiaries, pursuing a common business strategy in order to achieve a common interest, justifying the parent company's exercise of uniform management of the subsidiary or subsidiaries**.

At the core of the planned amendments is the assumption that, in addition to their own interests, companies being members of a corporate group should also pursue the corporate group's interests (i.e., a common business strategy), insofar as it aims to harm creditors or the subsidiary's minority partners or stockholders. **This is a significant departure from the traditional perspective of Polish companies law, according to which each company should first and foremost pursue its own interests and not the interests of the capital group to which it belongs**.

Among the amendments proposed is the repeal of Art. 7 CCC which regulated management agreements in respect of subsidiaries (contractual holding). In light of this amendment, the holding law as drafted would be based entirely on common institutions for both de facto and contractual holdings.

According to the draft bill, corporate groups will be able to benefit from holding law provisions if their member companies satisfy specific formal requirements, i.e.:

a) the subsidiary's Shareholders' Meeting or General Meeting must adopt a resolution on its membership in the corporate group, indicating the parent company, by a three-quarters majority of votes, and
b) both the parent company and the subsidiaries must disclose their membership in the corporate group in the Polish Register of Entrepreneurs by making the appropriate entry in the register (where, in the case of parent companies with a foreign seat, it is sufficient that the subsidiary disclose its membership in the corporate group in its register, indicating the parent company).

The provisions of the holding law will only apply to a given company and the members of its corporate bodies after the membership of said company in the corporate group is registered and disclosed in the Register of Entrepreneurs.

Further, membership in a corporate group will cease as a result of either the subsidiary's Shareholders' Meeting or General Meeting adopting a resolution, under the same majority requirements as mentioned above, on ending its membership, or the parent company gives notice to the subsidiary that its membership has ended.

Companies being members of a corporate group will be required to state their membership in a corporate group in their notices and commercial orders as well as on their websites.

In the latest version of the draft bill, the provisions regulating the scope of corporate groups were amended. On the one hand, the current wording of the draft bill allows for the application of the provisions on corporate groups to companies related to the parent company, if provided for in the related company's articles of association or statute. On the other hand, the draft bill excludes subsidiaries being public companies, bankrupt companies or companies in liquidation, if they have begun the division of their assets, from its scope.

Moreover, in connection with the entry into force of provisions concerning a new form of commercial company – the simple joint-stock company (*prosta spółka akcyjna*) – on 1 July 2021, the draft bill amending the CCC should be read in the context of Art. 4 §§ 2^1 and 2^2 pt. 1 CCC. Under these provisions:

a) the provisions on management boards and members of the management board should be, in principle, applied accordingly to simple joint-stock companies in which a board of directors is appointed;
b) wherever the CCC refers broadly to the stockholder's participation in the share capital, this should also be understood as the proportion of shares held by a simple joint-stock company's stockholder to the total number of shares of stock issued in such company.

If no further changes are made to the draft then, in effect, the provisions of the draft holding law, despite expressly referring to the concept of share capital and directly regulating the status of members of the management board in the corporate group, will also equally impact corporate groups in which simple joint-stock companies are members, even where a board of directors is appointed in such a company.

> Binding instructions of the parent company

According to the draft bill, the parent company will be entitled to issue binding instructions (in written or electronic form, under pain of invalidity) to its subsidiaries being members of the corporate group, in respect of the management of the company's affairs, if justified by the corporate group's interests. At a minimum, such instructions should state the:

a) actions which the parent company expects the subsidiary to take in connection with the performance of the binding instructions,
b) corporate group interest justifying the subsidiary's performance of the parent company's instructions,
c) expected benefit or harm to the subsidiary being a consequence of its performance of the parent company's instructions, and also
d) the manner and time in which the harm suffered by the subsidiary as a result of its compliance with the parent company's instruction is foreseen to be remedied.

The performance of binding instructions will require the prior adoption of a resolution of the subsidiary's management board containing, at least, those parts of the binding instructions referred to above. The subsidiary will also be required to notify the parent company of the adoption of such a resolution, or its refusal to perform the binding instructions.

A subsidiary may consider refusing to perform binding instructions in the following circumstances:

a) performing the instructions would result in its insolvency, or the threat of insolvency,
b) in the case of companies other than those wholly owned and where the articles of association or statute do not provide otherwise – also in the case of justified concerns that the instructions are contrary to the interests of said company and that the company would suffer harm which would not be remedied by the parent company or another subsidiary being a member of the corporate group within two years from the event causing said harm.

In the latter case, the management board, when assessing the potential harm to the subsidiary which may result from its performance of the binding instructions, will need to take into account the benefits achieved by that time on account of the subsidiary's membership in the corporate group.

According to the draft bill, a resolution refusing to perform binding instructions should be made prior to their performance and should include a justification. Note that the draft bill provides for the possibility to reserve additional conditions for refusal in a company's articles of association or statute.

> Parent company liability for the results of binding instructions

Parent companies will be liable for compensatory damages towards subsidiaries being members of the corporate group for the results on their performance of the parent company's binding instructions. Such liability, based on the principle of presumed fault, will arise if the harm is not remedied within the period indicated in the instructions. At the same time, with respect to wholly-owned subsidiaries, the parent company's liability will be narrower and limited to cases where the performance of binding instructions caused the subsidiary's insolvency.

The liability of the parent company will be determined taking into account its duty of loyalty to the subsidiary in issuing and performing the binding instructions.

To the extent provided for in the draft amendments, the parent company will also be liable to a subsidiary's creditors and minority partners (shareholders) for the results of the subsidiary's performance of its instructions.

> Liability of members of group companies' governing bodies

Members of the management board, supervisory board and audit committee, as well as commercial proxies and liquidators, of companies being members of a corporate group will be entitled to rely on the fact that their acts or omissions were undertaken in pursuit of a specific corporate group interest, provided that the company disclosed its membership in the group in the National Court Register.

As a rule, members of the management board, supervisory board and audit committee, as well as liquidators, of a subsidiary will not be subject to civil liability for harm caused by the performance of the parent company's instructions. However, provisions regulating the exclusion of such persons criminal liability were not included in the draft bill. We would note that, for example, in the case of the act stipulated in Art. 299 of the Criminal Code, it will not be possible to claim that a person acting as instructed failed to properly perform their duties or acted in excess of their authorization insofar as those actions resulted from the instructions themselves. From this perspective, it would not be possible to impose criminal liability.

> Protection of the parent company

The draft bill provides for a protection mechanism for the parent company, allowing it to effectively manage the corporate group, by permitting it to undertake a compulsory buy-out of the shares (stock) held by minority partners (shareholders) in its subsidiaries (a so-called 'squeeze-out'). This mechanism can also be applied to subsidiaries being limited liability companies (*spółki z ograniczoną odpowiedzialnością*) (which is a novelty in comparison to the law as it currently stands) as well as simple joint-stock companies (which will result from the incorporating reference in Art. 4 § 2^2 pt. 1 CCC).

Parent companies will be entitled to, at any time, review the books and documents of subsidiaries being members of the corporate group at any time and to request information from them.

A parent company's supervisory board (or, in its absence, the management board) will, as a rule, exercise ongoing supervision over the pursuit of the corporate group's interests by subsidiaries being members of the corporate group.

> Protection of minority partners (shareholders)

The annual management board reports on the activities of subsidiaries being members of the corporate group will be required to include an additional part concerning the contractual relationships between the subsidiary and the parent company for the previous financial year, indicating the binding instructions issued by the parent company to the subsidiary. Alternatively, such information may be included in a separate management board report.

Furthermore, minority partners or shareholders of subsidiaries being members of a corporate group which hold, alone or jointly with the company's other partners or shareholders, at least one-tenth of its share capital, shall be entitled to demand that the registry court appoint an audit firm to audit the accounting and activities of the corporate group.

The draft bill allows for the possibility for a subsidiary's minority partners (shareholders) to demand the compulsory purchase of the shares or stock they hold (a so-called 'sell-out').

Strengthening the position of supervisory boards

> Supervisory boards granted additional competences

In order to perform their duties, supervisory boards will be entitled to demand that the management board, commercial proxies, and all persons employed by the company (including persons employed under civil law agreements), provide any and all information, documents, reports and/or explanations necessary to supervise the company, in particular those concerning the company's activities or assets, also with respect of subsidiaries or related entities. Non-executive directors of simple joint-stock companies will have analogous rights, where a board of directors is appointed with a distinction between the functions of executive and non-executive directors.

Supervisory boards will be authorized to adopt resolutions requiring that specific issues related to the company's activities or its assets be audited (at the company's cost) by an auditor of their choice, provided that such entity possesses the necessary professional expertise and qualifications to examine a given matter.

A duty, based on that applicable to joint-stock companies, will be introduced requiring that the consent of the supervisory board be obtained for a company to enter into transactions with its parent company, subsidiary or a related entity, if the total value of transactions with the same entity during a given financial year exceeds 10% of the company's total assets, calculated on the basis of its most recently approved financial statements.

Moreover, the draft bill would amend the provisions on limited liability companies and joint-stock companies such that they expressly allow for the establishment of *ad hoc* or permanent committees within the supervisory board to perform specific supervisory functions (supervisory board committees). This will result in the harmonization of the legal regime applicable to all three forms of commercial companies, since, under the current version of the CCC, the ability to establish committees in a body is only expressly regulated in respect of simple joint-stock companies.

> **Additional duties of management boards**

According to the draft bill, management boards will be required to provide supervisory boards with additional information on a range of specified matters, including material transactions, resolutions adopted by the management board, and changes to the company's situation, without being called to do so. This mechanism is implemented in the CCC only in respect of joint-stock companies, however, note that the proposed provision may serve as a regulatory template which could be voluntarily added to the articles of association of a limited liability company or simple joint-stock company.

The draft bill provides for the imposition of criminal penalties on members of the management board, in the form of fines, limitation of their liberty if they fail to provide the supervisory board with the required documents and/or information, and also expands the catalogue of persons prohibited from acting as members of the governing bodies of capital companies to include persons convicted for the above offence.

> **Supervisory board reports**

The duties of supervisory boards will now include the preparation and submission of an annual written report on their activities for the previous financial year (the supervisory board report) to the partners' (or shareholders') meeting or the general meeting.

In addition to an assessment of the company's situation, a joint-stock company's supervisory board report shall also include an evaluation of the company's control and risk management procedures and an evaluation of the management board's compliance with its duty to provide documents and information. In respect of other forms of capital companies, the scope of information to be included in such reports has been left to the companies themselves.

Other changes

> The terms of office of members of the governing bodies of limited liability companies and joint-stock companies will be calculated by complete financial years (unless the articles of association or statute do not provide otherwise), which will resolve the current doubts in practice regarding the period of time for which members of such companies' governing bodies perform their functions.

> It will now be possible to engage the services of a professional advisor when carrying out qualification proceedings in respect of members of the management board in limited liability companies and joint-stock companies.

> Furthermore, following the example of the current provisions on simple joint-stock companies, the draft bill provides for:

- the codification of the duty of loyalty in the relationship between a limited liability companies and joint-stock companies and the members of their governing bodies,
- a more precise scope of the non-disclosure duty in the relationship between a limited liability companies and joint-stock companies and the members of their governing bodies – the prohibition on the disclosure of a company's business secrets will also continue to be effective following the end of a members mandate in a governing body,

- the introduction of the business judgment rule with respect to the compensatory liability regime applicable to members of the governing bodies of limited liability companies and joint-stock companies. This rule is based on the exclusion of liability for harm caused to the company as a result of decisions which turned out to be faulty, provided that they were taken within the limits of reasonable business risk and were based on adequate information under the circumstances.

Planned entry into force

The draft bill provides for a 6-month *vacatio legis*, as it is necessary for companies to amend their articles of association (statutes) to comply with the new legal regime.

If you have any questions related to any of the topics above, please contact the lawyers from our corporate law and corporate governance team:

Anna Wojciechowska
attorney-at-law, partner
anna.wojciechowska@wkb.pl

Anna Fennig
advocate
anna.fennig@wkb.pl

Krzysztof Wawrzyniak
advocate
krzysztof.wawrzyniak@wkb.pl

Legal basis:

Draft bill to amend the Commercial Companies Code and certain other acts, submitted to the Polish Parliament on 23 August 2021.