



# The Insolvency Law of Central and Eastern Europe

Twelve Country Screenings of the New Member and Candidate  
Countries of the European Union and Russia: A Comparative Analysis

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## VIII. Poland

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## 1. Introduction

### a) Historical Background

In Poland regulations on bankruptcy<sup>399</sup> and composition<sup>400</sup> proceedings from 1934 remained in force after the beginning of transition in 1989. Since these regulations had not been applied under socialist rule, after several amendments to original regulations – which proved to be insufficient – a fundamental reform became the main issue of discussion only in the middle of the nineties. Five years had passed since the last substantial amendment from 1997 before a completely new version of the insolvency law<sup>401</sup>, containing regulations on both bankruptcy and composition proceedings, was adopted.

Composition proceedings have played only a subordinate role until recently i.a. due to the exclusion of several categories of claims (e.g. tax claims, claims concerning social security contributions, salary claims of employees, claims arising from obligations secured by mortgage or pledge).<sup>402</sup> Although the new law promises improvement regarding this aspect, the following paper confines itself - i.a. because of a relatively small number of petitions with the aim of arrangement - to presenting basic features of arrangement proceedings. Special provisions of the insolvency law concerning e.g. state-owned enterprises, co-operatives or insurance companies, special regulations such as regulations on arrange-

<sup>399</sup> Dz. U. 1934, no. 93, pos. 834; 1991, no. 118, pos. 512; 1994, no. 1, pos. 1; 1995, no. 85, pos. 426; 1996, no. 6, pos. 43, no. 43, pos. 189, no. 106, pos. 496, no. 149, pos. 703; 1997, no. 28, pos. 153, no. 54, pos. 349, no. 117, pos. 751, no. 121, pos. 770, no. 140, pos. 940; 1998, no. 117, pos. 756; 2000, no. 26, pos. 306, no. 84, pos. 984, no. 94, pos. 1037, no. 114, pos. 1193; 2001, no. 3, pos. 8 as well as 2004, No. 232, Pos. 2338 (Bankruptcy Act).

<sup>400</sup> Dz. U. 1934, no. 93, pos. 836; 1950, no. 38, pos. 349; 1990, no. 55, pos. 320; 1996, no. 6, pos. 43 and no. 43, pos. 189 as well as 1997, no. 96, pos. 592, no. 121, pos. 770, no. 133, pos. 885 (Composition Act).

<sup>401</sup> Dz. U. 2003 no. 60, pos. 535 (Insolvency and Restructuring Law).

<sup>402</sup> On legal regulation according to the previous law see F. Zoll, A. Kraft, Overview of the Polish law on Composition proceedings, WiRO 2000, vol. 8, p. 273 et seq. (in German).

ment proceedings with banks or on protection of employees and their families in case of insolvency cannot be addressed here.

## **b) Insolvency Practice**

In the past, certain problems arose in insolvency practice that could not or could only partly be solved under the existing insolvency legislation, the Bankruptcy Act and the Arrangement Act. In particular, delays in filing the petition, duration of insolvency proceedings, their relative inefficiency and lack of reorganisation mechanisms were criticised by the insolvency judges, administrators as well as in legal publications.

While the number of submitted petitions first rapidly increased (4,193 in 1994), the number of opened bankruptcy proceedings has decreased from originally 23% in 1991 to about 19% in 1994. In the following years, the number of petitions declined and has remained at a stable level of about 2,700 from 1995 until 1998, while the percentage of proceedings which were opened and completed stayed at roughly 25%. Since 2000, the percentage has fallen to about 17%, whereas the number of petitions has risen considerably. E.g. in 2002, 6,814 petitions were filed, but only 1,141 proceedings opened; 1,388 petitions were rejected because debtor's assets were insufficient for the payment of the expenses of liquidation; in 3,927 cases petitions were rejected on formal grounds or proceedings were terminated. On 1 October 2003, when the new law became effective the number of pending proceedings under the old Bankruptcy Act amounted to 3,538.<sup>403</sup>

A similar negative situation can be observed as far as composition proceedings are concerned: after considerable fluctuations in the first years of transition, the number of petitions between 1994 and 1999 amounted to 500 on average, with 327 petitions in 1997 being the deepest point. Since 2000, the number of petitions has increased significantly, and achieved the highest level of 2,014 in 2002. However, the number of completed proceedings is much higher (about 30%) as compared to bankruptcy proceedings. In 2002, 539 proceedings were

<sup>403</sup> Statistics can be downloaded from the server of the Polish Ministry of Justice (<http://www.ms.gov.pl>).

opened, 307 petitions rejected, 1.003 petitions were set aside for other reasons; the number of pending proceedings amounted to 855. On 1 October 2003, when the new law became effective the number of pending proceedings under the old Composition Act amounted to 855.

With the coming into force of the new law the number of filings increased rapidly to 4.105 in the last three months of 2003 and 10.794 in 2004; of these 3.213 were still pending at the end of 2004. In the three years of the new laws existence, however, the newly introduced proceedings for out of court restructuring remain largely unused. The reason seem to be, on the one hand, the complex prerequisites and, on the other hand the associated cost.<sup>404</sup>

### c) Reform Objectives

The problems described above lead finally to the preparation of a completely new regulation of insolvency proceedings; the new Insolvency Law became effective on 1 October 2003.<sup>405</sup> The Insolvency and Reorganisation Law (hereinafter referred to as BRL) constitutes a uniform framework for all categories of proceedings, including insolvency and composition proceedings as well as preliminary reorganisation. It can be observed that the new Polish law was strongly influenced by the new German Insolvency Law, although the institute of consumer insolvency was not adopted by the Polish lawmaker. The main goals of the reform were to accelerate the insolvency proceedings, to enhance their efficiency and to offer possibilities of reorganisation and restructuring, while, at the same time, not neglecting protection of creditors.

Apart from the correction of a problematic limitation of the priority rights of secured creditors, introduced by the 1997 amendment to the Polish Bankruptcy Act, the new law introduced i.a. the following fundamental changes:

<sup>404</sup> See P. Wrześniewski „How much does the restructuring procedure cost“ (in Polish), in Rzeczpospolita of 1 January 2007, “Prawo i Gospodarka”.

<sup>405</sup> For a detailed analysis of the new law see F. Zedler, The Insolvency and Reorganisation Law – Introduction and Text, Zakamycze 2003 (in Polish).

- taking of evidence by experts within the opening proceeding (Art. 31 BRL);
- in the case of imminent illiquidity, reorganisation proceedings preceding insolvency proceedings (Art. 492 et seq.);
- enterprise takeover within the framework of a liquidation arrangement as an additional reorganisation instrument (Art. 271 BRL);
- elimination of separation in Insolvency Act and Composition Act and the possibility of changing between insolvency proceedings and composition proceedings;
- the possibility of discharge of residual debt of personally liable debtors within the insolvency proceedings (Art. 369 et seq. BRL);
- introduction of compulsory preliminary measures for protection of debtor's assets ex officio (hitherto only upon creditor's application); appointment of a preliminary court supervisor (Art. 36 et seq. BRL).

There are three possible proceedings according to the BRL: reorganisation proceedings (1) and insolvency proceedings which – depending on the content of the petition – are aimed either at liquidation (2) or at an composition (3) and can be conducted by the debtor's managers (a) or by an independent person appointed by the court (b). Proceedings, which were opened before 1 October 2003<sup>406</sup>, are conducted according to the previous Law; on proceedings concerning disqualification of an entrepreneur or legal entity, the new law shall be applied if the petition was filed after 1 October 2003. After three years of practical experience with the new law the Ministry of Justice currently prepares for a novel, targeting - amongst others - at relaxing the conditions of the restructuring procedure and correcting erroneous definitions.

<sup>406</sup> Decision of the Supreme Court of 5 February 2004 File no. III CZP 111/03; for details see Monitor Prawniczy 19/2004 (in Polish), p. 900 et seq.

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### a) Principles of Procedure and Legal Protection

The new Polish BRL is based on two fundamental principles: the principle of the most advantageous realisation of debtor's assets in order to satisfy creditors' claims, on the one hand, and the principle of "predominance of creditors' group interests", i.e. subordination of interests of individual creditors to the interests of creditors as a group, on the other hand. The functions of the insolvency proceedings are the following:

- (1) Reorganisation, e.g. restructuring of enterprises in the case of imminent illiquidity as well as of insolvent enterprises;
- (2) Vindication, i.e. just distribution of the proceeds from realisation of debtor's assets among the creditors;
- (3) Prophylaxis, i.e. prevention of further increase of the amount of debt by opening the insolvency proceedings;
- (4) Discharge of residual debt at least for certain categories of debtors;
- (5) Education of economic operators through a system of sanctions and incentives with the aim that operators should act as honest entrepreneurs.

Pursuant to references in Art. 35 and 229 BRL, the provisions of the Code of Civil Procedure are applicable as subsidiary regulations, unless the law provides otherwise. These provisions mainly govern rejection of judges, legal capacity to sue and to be sued, representation in court proceedings, exemption from the payment of procedure costs, service, procedural terms as well as rules of evidence and rules of appeal. Generally, the court has more powers under the special provisions of the BRL, whereby the principles of formality and of prevalence of written form are strengthened and the principles of party disposition and of public trial are weakened. Although in the case of Preliminary Reorganisation (Art. 492 et seq. BRL) proceedings are mainly conducted out of court by the entrepreneur under the general supervision of the court, provisions on insolvency proceedings concerning the petition (Part 1 Title II) as well as concerning the conclusion of a composition – which has to be confirmed by the court – are to be applied according to references in the legal provisions. The proceeding costs are now defined in

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Art. 230 BRL; the creditors have to make an advance payment of proceeding costs, if it is deemed necessary.

The court regularly decides by order (Art. 219 BRL) in a closed hearing (Art. 214 BRL), with the exception of cases in which a regular hearing is stipulated by law (e.g. Art. 259, 287 BRL). Contrary to the provisions of the Code of Civil Procedure, the court may order to conduct investigations and to collect evidence *ex officio* (Art. 218 BRL). All crucial decisions in the different procedures including out of court restructuring are published in the District Court Register.<sup>407</sup> The judge-commissioner decides if the parties submit a complaint against the actions of the administrator, court supervisor or trustee (e.g. preparation of the table of creditors' claims, Art. 256 et seq. BRL). Against the decisions of the judge-commissioner and of the trial court, an appeal can be lodged within 7 days after announcement or service. This procedure is time-sparing and less formal than a regular appeal (Art. 33 and 222 et seq. BRL).<sup>408</sup>

Although Poland reintroduced appellate courts in 1990 and re-established a structure of four levels of courts including three types of court proceedings, namely trial, appeal and cassation,<sup>409</sup> the legal protection in insolvency law is limited to a minimal control of the court, in order to achieve the needed acceleration of insolvency proceedings. Especially the procedure of appeal is tightened because of the executionary character of the insolvency law. Appeal against decisions of the

<sup>407</sup> See Law on the District Court Register of 20 August 1997, Dz. U. 2001 no. 17, pos. 209, no. 110, pos. 1189; 2002 no. 1, pos. 2, on. 113, pos. 984 and 2003 no. 49, pos. 408, no. 60, pos. 535 and no. 96, pos. 874 as well as Ordinance 00/1237 on the organisation of the District Court Register (as amended by Ordinance of 17 October 2003, Dz. U. no. 186, pos. 1821). For detailed information on the register see L. Cziulkin, Register of insolvent debtors, *Monitor Prawniczy* 2001, no. 18, p. 918 et seq. (in Polish).

<sup>408</sup> A good overview provides D. Zienkiewicz „The Appeal in Insolvency Matters“ (in Polish), *Monitor Prawniczy* 9/2006 p. 503 et seq. For detailed analysis of the reform of appeal see S. Gurgul, *Insolvency and Composition law – Commentary*, Warszawa 2000, Godlewska, Art. 17, Items 1-70 (in Polish).

<sup>409</sup> For general information on court system reform in Poland see U. W. Schulze, Country report Poland, in: H. Müller / G.-S. Hök / U. W. Schulze (eds.), *German writs of execution abroad*, p. 27 et seq. (in German).

judge-commissioner must be filed at the county commercial court (rayon court) that appointed the judge-commissioner; the court that conducts the insolvency proceeding thus performs the function of the court of second instance (Art. 222 § 1 sentence 2 BRL).<sup>410</sup> Nevertheless, the Constitutional Court ruled that Art. 109 BRL (termination of rent and lease contracts by the administrator on grounds of an order of the judge-commissioner) is unconstitutional in as far as it does not permit the control of the order by a court.<sup>411</sup>

Cassation against decisions of the courts of second instance, which is similar to the German revision procedure, is allowed only in specific cases (Art. 223 BRL): in case of discharge of the remaining debt (Art. 370 § 2 BRL) and in case of debtor's disqualification (Art. 376 no. 3 BRL).<sup>412</sup>

## **b) Scope and Applicability**

In the 1997 amendment to the Polish Bankruptcy Act, the term entrepreneur was introduced within the framework of insolvency law. The new BRL refers to the definition of this term in the Law on the Right to Economic Activities.<sup>413</sup> Pursuant to Art. 5 § 1 BRL, the insolvency law is applicable to physical persons or legal entities as well as to parts of legal

<sup>410</sup> See also D. Czajka, *Insolvency and Composition*, Warszawa 1998, p. 20 et seq. (in Polish); however, exemptions from this solution had to be introduced due to the decision of the European Court for Human Rights *Werner vs. Poland* from 15 November 2001 on appointment and dismissal of administrators, court supervisors and trustees (Art. 172 § 1 sentence 3).

<sup>411</sup> Verdict of 14 March 2006, File no. SK 4/05, Dz. U. no. 47, pos. 347; with respect to cases under the old law and the same grounds Verdict of 18 October 2004, File no. P 8/04, Dz. U. no. 232, pos. 2338 ruled Art. 101 § 3 Bankruptcy Act unconstitutional and, by amending Art. 538 para. 2 BRL, declared Art. 31 § 5 s. 2 Settlement Act as unapplicable.

<sup>412</sup> According to the previous law, cassation was also possible in case of rejection of appeal concerning court order on opening the insolvency proceedings, in case of amendments to such orders, in case of rejection of appeal on insolvency or composition petition or in case of confirmation of a (compulsory) composition (Art. 17 § 3, 193 Bankruptcy Act; Art. 24 § 3 and 66 Composition Act).

<sup>413</sup> Law from 9 November 1999, Dz. U., no. 101, pos. 1178; came into force on 1 January 2001.

entities which have no legal personality, but have legal capacity according to special regulations, if they perform economic or professional activities in their own name. The insolvency law is also applicable within the period of one year after the entrepreneur has died, or one year after cancelling the registration in the register at the district court if the entrepreneur has suspended his business activities. If the entrepreneur does business without registration, the law is, nevertheless, applicable. Further, the BRL can be applied to limited liability and joint-stock companies which do not perform economic activities, representations of foreign banks in the sense of the Law on Banks as well as to partners of partnerships whose personal liability is unlimited. The fact that partnerships are explicitly mentioned is attributable to the so called "limping legal personality" of partnerships according to Art. 8 of the Law on Commercial Legal Entities.<sup>414</sup> For that reason, insolvency of a partnership does not necessarily lead to the insolvency of partners.<sup>415</sup>

The problem of the legal personality of non-trading partnerships and, in this connection, the problem of applicability of insolvency law to such partnerships has been controversial until the end of 2002. After confirming the insolvency capacity in two decisions (II CZP 61/93, I CRN 6/95)<sup>416</sup> by reference to the acquiring of legal personality, the Supreme Court denied the legal status of a non-trading partnership in other decision (III CZP 11/95),<sup>417</sup> without expressing any opinion regarding insolvency capacity. Pursuant to Art. 2 § 3 of the Law on the Right to Economic Activities, partners, but not partnerships are deemed entrepreneurs. In consequence, the Supreme Court decided recently (III CZP 67/00)<sup>418</sup> that non-trading partnerships do not have insolvency capacity, so that property of partners constitutes debtor's assets.

<sup>414</sup> For detailed description of this problem see M. Jasiakiewicz, Who is liable for what?, *Rzeczpospolita* from 27 March 2002, *Prawo co dnia* (in Polish).

<sup>415</sup> The legal situation was the same under the previous law, whereby Art. 6 of the Bankruptcy Act contained an explicit regulation.

<sup>416</sup> Decision from 27 May 1993, File no. II CZP 61/93, OSNCP 1994, pos. 1, and decision from 21 February 1995, File no. I CRN 6/95, OSNCP 1995, pos. 102.

<sup>417</sup> Decision from 26 January 1996, File no. II CZP 11/95, OSNCP 1996, pos. 63.

<sup>418</sup> Decision from 6 November 2002, cit. in *Rzeczpospolita* from 19 November 2002, *Prawo co dnia*.

According to Art. 6 BRL, the following entities are excluded from the scope of application of the BRL:

- the state;
- autonomous local government entities;
- public autonomous health care entities;
- institutions and legal entities established by law or in the course of implementation of an obligation stipulated by law;
- physical persons who are farmers;
- schools.

The formulation “in the course of implementation of an obligation stipulated by law” which was inserted during the debate in the Senate is questionable, since it leads to a considerable extension of exemptions.<sup>419</sup> The list of exceptions from the applicability has 73 positions and embraces even private legal entities, which were founded without participation of the state or municipalities, solely because they were granted public status.<sup>420</sup>

### **c) Grounds for Opening Insolvency Proceedings**

Both illiquidity and over-indebtedness constitute grounds for opening insolvency proceedings under the BRL. With regard to illiquidity<sup>421</sup>, according to Art. 11 § 1 BRL, it is sufficient that the debtor “does not pay his debts as they fall due” for the court to open the insolvency proceedings. Also in case of temporary cessation of payments or of a small

<sup>419</sup> This concerns e.g. the state-owned enterprise Polish State Railways which was converted into the joint-stock company Polish Railways PKP SA on the basis of the Law on Commercialising, Restructuring and Privatisation of the State-owned Enterprise Polish State Railways from 8 September 2000, Dz. U. 84, pos. 948, no. 100, pos. 1086 and no 2154, pos. 1802, 2002, no. 205, pos. 1730.

<sup>420</sup> See the list with a commentary in M. Przychodzki / K. Sącińska The Lack of Applicability of the Insolvency Law for Public Legal Entities (in Polish), *Przegląd Prawa Handlowego* April 2006, p. 27 et seq.

<sup>421</sup> For the definition see M. Pannert, “Illiquidity as a Ground for the Opening of Insolvency Proceedings” (in Polish), *Monitor Prawniczy* No. 16/2004, p. 733 et seq.

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amount of debt the proceedings can generally be opened. However, it is possible to reject the petition in such cases according to Art. 12 BRL, if the delay of payment is not longer than three months and/or if the amount of due debts is not higher than 10% of the balance value, provided that the delay is not for a long period and the rejection does not endanger creditors.

The criterion of over-indebtedness laid down in Art. 11 § 2 BRL is only applicable to legal entities and to parts of legal entities which have no legal personality, but have legal capacity according to special regulations. It is based on an abstract assessment concept calculated mathematically. This factor triggering insolvency, seen as a compensation of the limited liability of companies, needs transparent, measurable and verifiable criteria in order to be efficient and enable the management to exercise control over company's liquidity and viability. However, the abstract criterion, used in the BRL, according to which "liabilities exceed assets", does not accurately reflect the economic status of a company and is unpractical.<sup>422</sup> In this context the introduction of taking of evidence by experts in the opening proceedings under the BRL (Art. 31) is a step in the right direction and may help to develop the criterion of over-indebtedness.

Grounds for rejection of the petition in case of insufficiency of debtor's assets were extended in the 1997 amendment to the Bankruptcy Act, so that a petition had to be rejected if, after deducting the value of the objects by which creditors secured their claims from the value of all assets, the remaining amount was not sufficient for covering the cost of proceedings. This extension is now qualified by Art. 13 BRL. The court has to examine if the encumbrances and other claims diminishing the debtor's assets are valid under the BRL or were established to damage creditors.

<sup>422</sup> This raises the question whether over-indebtedness should be assessed only mathematically or a negative forecast regarding the prospects of the company should also be considered, as it is the case in the current German legislation.

**d) Persons Entitled and Persons Obligated to File the Petition**

The BRL mentions - apart from the debtor, a creditor, the liquidator of legal entities and trading companies - partners of partnerships, persons authorized to represent legal entities or parts of legal entities, and, in the case of state-owned enterprises, the establishing authority or the body authorized to represent the Treasury. In certain cases, an appointed guardian or a state organ granting subventions also can file the insolvency petition. According to Art. 21 § 1 BRL, the obligation to file the petition by the debtor must be complied with within 14 days of the cessation of payments or of continuous over-indebtedness. This obligation was extended by the 1997 amendment to the Bankruptcy Act<sup>423</sup> and, additionally, by the BRL, so that the debtor filing the petition has to submit an updated inventory of his assets including estimated valuation, information about all pending court and administrative proceedings and a declaration about the truthfulness of provided information according to Art. 22 BRL. In this connection, provisions of Art. 28 et seq. BRL stipulate that the petition can be rejected if the debtor's petition does not comply with the requirements of the law or if the debtor's address given in the petition is incorrect are problematic.<sup>424</sup>

In case of delay in filing the petition, the debtor or legal representatives of legal entities are not only liable for damages according to Art. 21 § 3 BRL, Art. 299 et seq. of the Law on Commercial Legal Entities (for limited liability companies) and Art. 479 et seq. of the Law on Commercial Legal Entities (for joint-stock companies), but may also be subject to

<sup>423</sup> The following documents were to be submitted by the debtor filing the petition: the balance sheet, the list of creditors and securities as well as of the claims satisfied in the last 6 months.

<sup>424</sup> This risk outweighs incentives to file the petition early and has a negative impact on the situation of creditors; see D. Niedzielska in *Rzeczpospolita* from 28 January 2003, *Insolvency petition, annex Dobra Firma* (in Polish).

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interdiction of participation in economic activities in executive positions for a period of three to ten years pursuant to of Art. 373 et seq. BRL.<sup>425</sup>

Disqualification is also applied if these persons do not fulfil their obligation to give information and to co-operate or if they destroy, hide or encumber the debtor's assets after the petition was filed, further, if the last insolvency proceedings were conducted less than five years ago or the remaining debts were discharged at least once.

Disqualification includes interdiction of doing business as an individual entrepreneur and of exercising functions of an executive officer as well as interdiction of exercising functions of a member of the supervisory board. This rule is to be applied also to foundations and associations. The proceedings are introduced only on the basis of an application of a creditor, administrator, court supervisor or trustee as well as of the president of the Consumer Protection Office and the chairman of the Securities and Stock Exchange Commission and conducted as a special proceeding with the possibility of cassation according to the provisions of the Code of Civil Procedure (Art. 376 BRL). The court takes into consideration the degree of fault, loss of value of the enterprise as well as the amount of creditors' damage. Disqualification is registered *ex officio* in the register of insolvent debtors at the district court according to Art. 55 § 4 of the Law on District Court Register.<sup>426</sup>

The introduction of liability of a person filing a petition in bad faith for damage to the debtor or to third persons if the unfounded petition is rejected is a further new feature (Art. 34 BRL). In addition to the compensation of damage, the court can oblige the creditor to inform the public of his actions. The question if one single creditor is sufficient for opening of the insolvency proceedings or whether this contradicts the principle of complete execution is unfortunately left open by the Polish insolvency law. This remains a controversial issue and the pre-war

<sup>425</sup> Hitherto three to five years pursuant to Art. 17 § 2 of the Bankruptcy Act. The compliance of this norm with the Constitution was confirmed by the decision of the Constitutional Court which argued that disqualification is not a sanction, but an instrument for protection of public interest in this case. The decision is published in *Dz. U.* 2002, no. 113, pos. 990.

<sup>426</sup> According to a decision of the Supreme Court of 19 February 2003 File no. V CK 7/03 by the Register Court without a regard to the motives; see *Monitor Prawniczy* 19/2004, pp. 907 (in Polish).

jurisprudence and legal literature concerning this topic are frequently cited. There are strong arguments for allowing such petitions.<sup>427</sup>

### 3. Institutional Framework

#### a) Court, Judge-Commissioner

In Poland, cases concerning insolvency and composition proceedings are within the subject-matter jurisdiction of commercial courts at the county (rayon) courts (Art. 18 BRL).<sup>428</sup> Proper venue is determined by the location of the main enterprise of the debtor (Art. 19 BRL). If there is no enterprise, debtor's office or domicile or location of assets are sufficient. If there are several enterprises located in different counties, petition can be submitted to one of the respective county courts chosen by the petitioner. Thus, almost all proceedings against the debtor, including proceedings on the validity of encumbrances, are conducted at the same court. Only actions for rescission are to be raised – depending on the amount in dispute – at a court according to the general rules on jurisdiction.

In the decision on opening of the insolvency proceedings, in which the aim of proceeding (liquidation or composition) has to be determined, the court shall appoint from among three judges a judge-commissioner to supervise the proceedings and activities of the administrator

<sup>427</sup> With regard to the discussion see P. Nazarewicz, Opening the bankruptcy proceedings against a business entity with one single creditor (in Polish), *Przegląd Prawa Handlowego* August 1997, p. 10 et seq.

<sup>428</sup> For further details see A. Pokora, Jurisdiction in the insolvency proceedings, *Przegląd Prawa Handlowego*, October 1997, p. 11 et seq. (in Polish).

or of the court supervisor.<sup>429</sup> The judge-commissioner is authorized to adopt all decisions on behalf of the court, unless it is expressly stipulated by law that the court has to decide in a matter (Art. 151 BRL). Apart from disputes on remuneration of the administrator, court supervisor or trustee and appeals against decisions of the judge-commissioner, which are exempted (Art. 150 BRL), after the decision on opening of the insolvency proceedings, one professional judge decides on behalf of the court (similar to the provision of Art. 47 of the Code of Civil Procedure). Only the court is authorized to decide on opening of the insolvency proceedings, whereby it is obliged to make a decision within two months after it has determined that the petition meets the requirements stipulated by law (Art. 27 § 3 BRL).<sup>430</sup> In case of an appeal, the appellate court can only remit the case to the lower court (Art. 54 BRL).

#### **b) Administrator, Court Supervisor, Trustee, Guardian**

If the insolvency proceeding is opened with the aim of liquidation, the court appoints an administrator, who takes over the debtor's assets *ipso iure*, administers and realises them according to Art. 173 BRL. If the insolvency proceeding is opened with the aim of composition and managers of the debtor are not dismissed by the court, the court appoints a court supervisor; if managers of the debtor are dismissed, the court appoints a trustee. As a result of the introduction of compulsory preliminary measures for protection of debtor's assets *ex officio* (Art. 36 et seq. BRL), the court regularly appoints a preliminary court supervisor; other measures, e.g. receivership, can also be ordered.<sup>431</sup> According to the prevailing opinion, administrators, court supervisors and trustees are

<sup>429</sup> A more detailed study by P. Pogonowski, Powers of the judge-commissioner in the bankruptcy proceedings, *Przegląd Prawa Handlowego*, November 1998, p. 22 et seq. (in Polish).

<sup>430</sup> Already in the amendment of 1997, compulsory terms for phases of the proceedings were introduced in order to accelerate the proceedings.

<sup>431</sup> If a creditor files the petition, the court can order preliminary measures only if the creditor substantiated the grounds for opening the proceedings in his or her petition.

private persons performing official functions, e.g. preparation of the table of creditors' claims (Art. 244 pp. BRL).<sup>432</sup> Pursuant to Art. 160 BRL, they act on account of the debtor, but in their own name and are liable for damages resulting from breach of duty, but not for obligations they accept in the course of their work as insolvency practitioners.

As a rule, insolvency practitioners are selected from a list kept by the president of the court. In 2007 a special law<sup>433</sup> on licensing of these professionals, introducing at the same time compulsory insurance against civil liability for damages, was adopted. Apart from physical persons, partnerships may also be appointed, if their personally liable partners or executive officers authorized to represent the partnership possess such licence. The requirements include, among others, a university degree (not necessarily in law) and a good knowledge of commercial, civil, labour and financial, three years of professional experience law as well as a clear record of conviction.

A guardian ("curator", Art. 187 BRL) can be appointed in certain situations: for physical persons who can not sue and be sued and have no legal representatives, for legal entities without regular executive bodies or a liquidator, for a deceased debtor, if his successors do not join the proceedings, and for consumers in the insolvency of an insurance company (Art. 473 BRL) or of a company issuing securities (Art. 484 BRL).

### **c) Creditors' Meeting and Creditors' Committee**

Although the judge-commissioner still plays a key role in the insolvency proceedings, the position of creditors has been strengthened, whereby

<sup>432</sup> For an overview see D. Zienkiewicz / A. Świderek, „The Role of Administrator, Court Supervisor, Trustee, Guardian in Insolvency proceedings“ (Polish), Monitor Prawniczy no. 17/2004, p. 814 et seq. and 18/2004, p. 861 et seq.

<sup>433</sup> Law on the Licencing of Administrators, Dz. U. 2007, no. 123, pos. 850; before the law was adopted, requirements concerning professional qualification of physical persons and requirements concerning the capacity of legal entities to exercise these functions were laid down in an Ordinance of the Ministry of Justice from 16 April 1998, Dz.U. no. 55, pos. 359. Transitory rules are valid until 2010.

the principle of “predominance of creditors’ group interests” now prevails.<sup>434</sup> Creditors are represented by the creditors’ meeting which can be attended by all creditors whose claims are accepted whereby every creditor has one vote (Art. 195 BRL). Secured creditors and creditors whose claims to compensation arise from an employment contract or are confirmed by the decision of the court or of an administrative body can participate in the meeting without registering their claims with the responsible insolvency practitioner beforehand (Art. 236 BRL). Generally, the majority of creditors present at the meeting, provided that such majority represents at least 1/5 of the total claims, is sufficient for adopting decisions, irrespective of the number of persons present (Art. 199 BRL).

Before adopting the decision on opening of the insolvency proceedings, the court can – unless only the liquidation proceedings can be introduced for legal reasons – summon the so called first creditors’ meeting which shall decide whether the aim of the proceedings should be liquidation or composition. The creditors’ meeting can elect the creditors’ committee, which is an optional organ, and propose candidates for the position of administrator, court supervisor or trustee. Besides, an composition can be made already in the first meeting if the majority of creditors holding at least three quarters of all claims vote for that (Art. 45 BRL). In the further course of proceedings, creditors can decide on separation of property belonging to a third party (Art. 63 BRL), elect (if not elected before) the creditors’ committee or change of its composition (Art. 203 BRL) and, if they vote unanimously, on termination of proceedings (Art. 361 no. 3 BRL).

The creditors’ committee can also be set up by the judge- commissioner on his own initiative (Art. 45, 201 et seq. BRL). The creditors’ committee supports and controls the administrator and is entitled to approve decisions of the administrator in cases determined by law (Art. 206 BRL), e.g. on continuation of business for more than three months, on land sales without tender procedure, on taking out of loans or on

<sup>434</sup> The new regulations impose considerable restrictions on certain rights of individual creditors. In particular, in case of opening of the proceedings with the aim of composition it is now problematical to terminate contracts.

performance of contracts. If the creditors' committee was not established, the judge-commissioner exercises these functions.

## 4. Insolvency Proceedings

### a) Preliminary Reorganisation Proceedings

In the case of imminent illiquidity entrepreneurs who are registered at the district court<sup>435</sup> can apply for reorganisation at the proper court. Entrepreneurs who have conducted reorganisation within the last two years or have been subject to insolvency proceedings within the last five years are excluded. According to Art. 492 BRL, imminent illiquidity is given "if it is evident on the basis of a comprehensive analysis of the economic situation of the entrepreneur that the entrepreneur, although he or she still pays his debts, will become insolvent in a short time". Only the debtor can file the petition during this early phase. The proceedings are conducted out of court, but under supervision of the court whereby the debtor must remunerate the supervisor appointed by the court. Opening of the proceedings must be announced in a nationwide newspaper and in the Court and Economics Gazette.<sup>436</sup>

Opening of the proceedings whose duration should not exceed three months for small and middle-sized enterprises and four months for other debtors (Art. 519 BRL) has the following effects:

- Suspension of obligations for payments;
- Suspension of charging default interest;
- Restrictions on set-off;

<sup>435</sup> In case of an out-of-court settlement, creditors have access to information contained in the public register which is needed for adopting adequate decisions.

<sup>436</sup> Monitor Sadowy i Gospodarczy.

- Stay of execution proceedings and of seizure of property (but not of other proceedings, including the opening proceeding);
- Possible public appointment of an expert by the court for examination of the debtor's enterprise;
- Interdiction of further encumbrances on debtor's property or of realisation of debtor's property outside of the normal course of business.

Economic incentives for the debtor are, aside from the protection against creditors, the possibility to manage the enterprise independently under court supervision (Art. 497 et seq. BRL), proposition of a reorganisation plan in the petition (Art. 502 et seq. BRL) and discharge of residual debt as a result of the composition (Art. 504 et seq. BRL). However, this solution is problematic<sup>437</sup> because the extensive and imprecise definition of the ground for the petition and the fact that only the debtor can file the petition in this case could induce the debtor "to escape to insolvency" and thus to protect himself from execution of creditors' claims. Aside from that, the weak position of creditors in the reorganisation proceedings supervised by the court as compared to out-of-court reorganisation enables the debtor to threaten creditors with the "escape to insolvency" in order to force the creditors to make concessions in an out-of-court settlement which is not market-driven.<sup>438</sup>

The entrepreneur summons the creditors' meeting in co-operation with the court supervisor, who chairs the meeting, and proposes his composition plan there. The plan can contain propositions concerning restructuring of debts, assets as well as of human resources; an composition on discharge of debt should be made. As in the insolvency proceeding, creditors are generally divided in four groups, but they can also vote together. An composition is concluded if the majority of creditors (in case of voting in groups, majority of each group) who hold at least 2/3 of voting claims vote for it (Art. 510, 285 BRL). The composition will be then either approved or rejected by the court (Art. 514 et seq. BRL). Art.

<sup>437</sup> See also D. Niedzielska, Insolvency petition, Rzeczpospolita from 28 January 2003, Annex Dobra Firma (in Polish).

<sup>438</sup> See also C. Kirchner, Economic theory of insolvency law, Summary under <http://www.insolvenzverein.de/archiv/verastvorbei02/Arbeitsbl.htm>.

291 et seq. BRL is to be applied *mutatis mutandis* to the effects of court approval.

These proceedings have been applicable to large enterprises of special importance to the labour market<sup>439</sup> before the BRL became effective, since 24 April 2003, according to special regulations. Additionally, these enterprises with more than 1.000 employees could apply to the Ministry of Economy for restructuring of public and civil claims and to the Agency for Industrial Development for support of restructuring of loans and sureties until the beginning of 2003.<sup>440</sup>

### **b) Effect of the Commencing the Insolvency Proceeding**

According to the petition, management of debtor's assets is conferred on an administrator (proceedings with the aim of liquidation) or on a trustee (proceedings with the aim of composition). Only in case of proceedings with the aim of composition and without dismissal of debtor's managers, the debtor is allowed to manage his assets under control of the court supervisor whereby the debtor needs the approval of the supervisor for all property transfers outside of the normal course of business. Prerequisite is that the debtor became insolvent as a result of extraordinary circumstances which were not connected with his actions and he or she guarantees to be able to independent management; this regulation reminds of the regulation in the Composition Act.<sup>441</sup>

Generally, all execution proceedings (execution of court judgements and of administrative decisions) are to be stayed and – after the decision

<sup>439</sup> Law on public subventions for entrepreneurs of special importance to the labour market from 1 October 2002, Dz. U. no. 213, pos. 1800.

<sup>440</sup> The Ministry of Finance handled 54.520 of 60.378 applications for restructuring of tax liabilities amounting to 5,4 billion Zloty, Rzeczpospolita from 1 April 2003, The firm has problems, Annex Dobra Firma (in Polish). However, there were only 46 applications for loans or sureties, Rzeczpospolita from 23 April 2003, Reorganisation first for large enterprises (in Polish).

<sup>441</sup> According to the prevailing opinion, the term extraordinary circumstances according to the Composition Act was to be construed as circumstances for which the debtor is not liable irrespective of the fact if these circumstances were caused by processes within the enterprise or outside it.

on opening the insolvency proceedings – terminated (Art. 146 BRL). Claims against the debtor concerning assets which are part of the insolvency estate are not collectable by way of execution. In the proceeding with the aim of composition, claims which are excluded from the composition are not exempted from execution; with this being the only exemption (Art. 140 BRL). The judge-commissioner can order the stay of execution proceedings and of seizure of property for up to three months on the basis of an application or ex officio, with the exemption of proceedings on the basis of personal claims according to Art. 273 BRL.

Pursuant to Art. 61 et seq. BRL, the insolvency estate is composed of all assets which are owned by the debtor<sup>442</sup> on the day of opening of the insolvency proceedings and all assets which are purchased by the debtor during the insolvency proceedings, including debtor's claims on salary or similar claims. Property exempted from execution, part of income exempted from garnishment and property separated by the judge-commissioner or the creditors' meeting as belonging to a third party do not belong to the insolvency estate. In this context the separation right of the secured creditor in the bankruptcy of the party granting the security is acknowledged, whereas that of the party granting the security in the bankruptcy of secured creditor is disputed.<sup>443</sup> Apart from conferring management of the insolvency estate to an administrator or a trustee, there are other effects of the court decision on opening of the insolvency proceedings according to substantive law which serve the protection of the insolvency estate:

- Contracts concluded by the debtor and encumbrances granted by the debtor regarding the insolvency estate are null and void, unless the debtor is allowed to manage assets under court supervision (Art. 77, 81 BRL);

<sup>442</sup> General information on the rights and obligations of the debtor see A. Pokora, Status of the debtor in the insolvency proceedings, *Przegląd Prawa Handlowego* March 1998, p. 31 et seq. (in Polish).

<sup>443</sup> With a synopsis of the different opinions see S. Gurgul, „The Bankruptcy of the Entrepreneur-Beneficiary of a secured claim resulting from a Trustee relationship“ *Monitor Prawniczy* 12/2005, p. 735 et seq. (in Polish).

## VIII. Poland

- The debtor is not allowed to disclaim an inheritance after the court decision on opening of insolvency proceedings (Art. 119 et seq. BRL);
- The severance of joint property is not allowed after the court decision on opening of the insolvency proceedings. The dissolution of community of property within one year before the opening of insolvency proceedings is null and void (Art. 124 et seq. BRL).

Contract clauses according to which legal relations with the debtor should be dissolved or amended in case of insolvency are null and void ex lege (Art. 83 BRL).

### *aa) Opening of Insolvency Proceedings with the Aim of Composition*

Generally, neither the trustee nor the debtor are allowed to satisfy the claims which are part of an composition. However, claims which emerged after opening of the insolvency proceedings and claims which were inserted in the composition afterwards with the approval of creditors can be satisfied with the approval of the judge-commissioner, provided that it is necessary for continuation of business or it enhances the efficiency of the debtor's enterprise (Art. 88 BRL). According to the principles of most advantageous realisation and of "predominance of creditors' group interests", single creditors are not allowed to cancel rent, leasing and licence contracts as well as bank guarantees, bank account contracts, sureties etc. which are connected with the debtor's enterprise (Art. 90 BRL). To ensure the fulfilment of the composition, the set-off is prohibited according to Art. 89 BRL (as in Art. 39 of the Composition Act) if the creditor became debtor after the opening of insolvency proceedings or the creditor became creditor as a result of cessation after the opening of insolvency proceedings.

### *bb) Opening of Insolvency Proceedings with the Aim of Liquidation*

The effect of the opening of insolvency proceedings with the aim of liquidation (Art. 91 et seq. BRL), especially concerning different types of contracts such as sales contract, order and commission, agency, rent,

lending, loan as well as marriage contract<sup>444</sup>, is basically the same as in the Bankruptcy Act. However, several new types of contracts such as leasing, credit, administration or security contract are included in the new regulation. There are the following important general rules:

- All authorizations, powers of attorney and orders, as well as not accepted contractual offers become void;
- Unmatured claims regarding the insolvency estate fall due;
- The administrator can decide if contracts concluded, but not or only partly performed by the debtor should be performed or cancelled (Art. 97 et seq. BRL);
- Set-off is allowed only regarding the claims which could have been set off before the opening of insolvency proceedings (Art. 93 et seq. BRL).

Regulations of the Bankruptcy Act on mutual contracts and on lease contracts are substantially amended in the new law: if the administrator does not answer the request of the creditor concerning performance within three months his silence is to be interpreted as revocation of the contract. After opening the insolvency proceedings, the administrator is entitled with the approval of the judge-commissioner to terminate all lease contracts concluded with the debtor by lessees within three months, even if the lease term is unlimited, provided that the existing contract complicates the liquidation (Art. 109 BRL<sup>445</sup>).

There are also special provisions regarding the debtor's debts in the form of checks or bills of exchange. Upon the insolvency of the drawee, the holder of the bill of exchange has regressive claims against the other bill-of-exchange debtors, irrespective of the fact whether the drawee accepted the bill. Upon the insolvency of an issuer of checks, the drawee must deny the payment. In addition, special regulations exist, which complement the BRL, concerning labour relations, especially the continuation and termination of such relations.

<sup>444</sup> See S. Gurgul, „Bankruptcy and property relations between Spouses“, Monitor Prawniczy 6/2005, p. 279 et seq. (in Polish).

<sup>445</sup> In its Verdict of 14 March 2006, File no. SK 4/05, Dz. U. no. 47, pos. 347 the Constitutional Court ruled Art. 109 BRL as unconstitutional in as far as it does not permit the control of the order by a court.

If the aim of the proceedings changes, i.e. to facilitate an composition, the effects of the opening decision remain, unless the parties agree upon another course of action (Art. 117 BRL).

### **c) Rescission and Invalidity of Pre-Petition Transactions**

The administrator and the creditors<sup>446</sup> are entitled to request the court to declare all legal transactions of the debtor interfering with the satisfaction of their claims as void (action pauliana).

Rescission claims may be filed against legal transactions performed by the debtor<sup>447</sup> with the intention to damage the creditors. This procedure is governed by the provisions of Art. 527-574 of the Civil Code regarding the protection of creditors in case of the debtor's incapacity to make payments. The rescission is filed against the person favoured by the void action. The assets taken from the estate of the debtor following a void action must be returned to the debtor's estate according to Art. 134 BRL. If such return is not possible, adequate compensation has to be paid. The 1997 amendment of the Bankruptcy Act simplified the preconditions for the creditors' rescission in Art. 527 § 4 of the Civil Code: it is assumed that a creditor being in a permanent commercial relationship with a debtor and receiving a certain benefit of the debtor to the disadvantage of the other creditors, knew of the intention of the debtor to prejudice the other creditors. Before the amendment, the creditors had to deal with the difficult task<sup>448</sup> of proving the debtor's intention to prejudice them and the fact that the favoured person was aware of the debtor's intention, now the debtor must prove his good faith.

<sup>446</sup> In its Opinion of 13 May 2003 File no. V CK 63/02 and 1st Decision of 12 March 2003 File no. III CZP 85/02, the Supreme Court ruled that institutions, for whom the legislator foresees the administrative procedure shall have the same right; see (in Polish) *Monitor Prawniczy* 19/2004, p. 900 et seq.

<sup>447</sup> Pursuant to a Verdict of the Supreme Court from 29 November 2006 File no. III CSK 250/06 this may as well be a single partner of a commercial partnership; see in *Rzeczpospolita* of 2 January 2007 "Prawo i Gospodarka".

<sup>448</sup> For the aspects related to the revocatory action in the current legal situation see "The difficult task of the creditors", *Rzeczpospolita* from 26 May 1998 (in Polish).

Furthermore, all transactions free of charge or non-equivalent transactions operated by the debtor within the last year preceding the filing for bankruptcy as well as the securities pledged in the last two months (mortgages, pledges etc) in respect of immature claims become unenforceable against the insolvency estate according to Art. 127 BRL. This also applies to the legal transactions concluded within six months before the filing for insolvency by the debtor with his spouse or direct and collateral relatives down to the second degree, including children and adopted children, by the company with its associates or the associates' representatives or their spouses as well as between companies, if the company of the debtor dominates the other company. New is the authorization of the judge-commissioner ex officio or upon application of the administrator, court supervisor or trustee to declare a part of the remuneration of management staff of the debtor (executive officer, members of the board of directors, members of the supervisory council etc.) null and void in relation to the debtor's estate and thus to reduce it, if it exceeds the usual remuneration considerably and is not justified by extraordinary circumstances (Art. 129 BRL). Such course is also possible regarding encumbrances (pledge, mortgage etc) granted by the debtor within one year preceding the insolvency petition for which the debtor was not rewarded, unless the debtor became personally liable.

### **d) Composition**

The composition proceedings which were hitherto regulated as a settlement proceeding in the Composition Act and as a compulsory composition in the Bankruptcy Act is completely revised and now laid down in Art. 267-305 BRL. Prerequisite is that both, the procedure leads to a higher recovery rate as compared with liquidation and that the debtors previous behaviour gives rise to the expectation that he will fulfil the settlement.<sup>449</sup> Whereas previously a great number of categories of claims

<sup>449</sup> For an overview see Z. Miczek, „The legal Position of Creditors of non-monetary Claims in Insolvency Proceedings with the Aim of Settlement“ (in Polish), *Przełąd Prawa Handlowego* April 2005, pp. 4 et seq.; an automatic transformation into monetary Claims (comp. Art. 91 BRL) does not take place in this case.

were exempted,<sup>450</sup> the BRL extended the applicability considerably, so that salary claims of employees and claims arising from obligations secured by mortgage or pledge are not generally included, but can be included if approved by the respective creditors, Art. 273 para.3 BRL. The inclusion of claims secured by transfer of ownership already anticipated by case law<sup>451</sup> is now regulated by Art. 272 para. 1 BRL. This does not hinder the creditor though to seek satisfaction from the proceeds of the sale of the collateral transferred after the opening of the procedure but before the conclusion of the settlement; nevertheless, he has to return the sum exceeding his proportional claim according to the settlement as unjustified enrichment.<sup>452</sup> Only claims on alimony, some claims on annuity, claims concerning social security and pension insurance contributions, claims on separation of property, claims based on the inheritance accrued after the insolvency proceedings were opened as well as claims which were satisfied with the approval of the judge-commissioner (Art. 273 BRL).

The proceedings consist of three phases: proposition, conclusion and fulfilment of composition. If it is allowed to conclude an composition according to the court decision on opening the insolvency proceedings, the debtor, the court supervisor or the trustee can propose an composition within one month, in case of prolongation of the term within three months. Also if the proceedings are aimed at liquidation, the debtor, the administrator or the creditors' committee can propose an composition. However, if the composition proceedings are to be continued as the liquidation proceedings the composition proceedings cannot be repeated afterwards. As possible subjects of the composition, i.a. extension of payment, payment by instalments, remission of debt, debt-to-equity- swap, conversion of encumbrances and takeover of assets are mentioned whereby both restructuring and liquidation can be the ultimate goal of composition.

<sup>450</sup> E.g. tax claims, claims concerning social welfare contributions, salary claims of employees, claims arising from obligations secured by mortgage or lien, Art. 4 of the Composition Act.

<sup>451</sup> Decision of the Supreme Court of 11 September 2003 File no. III CZP 53/03.

<sup>452</sup> Compare also A. Jakubecki in a commentary to the cited decision (in Polish) *Monitor Prawniczy* 18/2004, p. 855 et seq.

Creditors allowed to vote are generally divided in four groups: secured creditors, employees and farmers as suppliers, shareholders or stockholders and other creditors. The conditions for debt restructuring must be the same within each group whereby minority creditors and new creditors can be privileged. Employees should obtain at least the minimum salary. An composition can be adopted by the majority of creditors<sup>453</sup> belonging to the respective group who hold at least 2/3 of voting claims (see Art. 285 and 510 BRL on reorganisation proceedings). In special cases, an composition can be adopted against the votes of a creditors' group on the basis of the decision of the judge-commissioner, provided that the majority in all other groups supports the composition and the situation of creditors in the opposing group is not worse than in case of liquidation.

The concluded composition is to be approved or rejected by the court after examination (Art. 287 et seq. BRL). After the court orders on approval of the composition and on termination of the insolvency proceedings become effective, the debtor will regain the right to administer and dispose of his assets with restrictions laid down in the composition. By the legal power of the court order on approval of the composition, all execution proceedings and proceedings concerning seizure of property concerning claims included in the composition are terminated, writs of execution are annulled *ex officio* on the day the court order becomes effective. The composition is binding regarding all claims identified in the BRL, irrespective of the fact whether the claims were included into the table of claims. Pursuant to Art. 298 BRL under exceptional circumstances that occur afterwards and alter the economic situation in a way that notably rises or reduces the income of the debtor enterprise an adaptation of a confirmed settlement upon request of one of the parties is possible.<sup>454</sup> After fulfilment of the composition, the court adopts decision on fulfilment of the composition upon application of the

<sup>453</sup> For the calculation of the majority in each group only those creditors are taken into account that have agreed that their claims are embraced by the settlement; see Decision of the Supreme Court of 29 November 2006 File no. III CZP 90/06, in *Rzeczpospolita* of 2. January 2007 "Prawo i Gospodarka".

<sup>454</sup> See A. Witosz „The *rebus sic stantibus* Clause in the BRL“ (in Polish), *Przeegl'd Prawa Handlowego* Januar 2006, p. 33 et seq.

debtor, the administrator or another person responsible for fulfilment of the composition. All registrations in public registers and lists are cancelled on the basis of the court decision, so that the debtor regains the right to administer and dispose of his assets without restrictions.

#### **e) Status of Secured Creditors**

After the entitlement of secured creditors to separate satisfaction of claims was eliminated and privileges for secured creditors according to the priorities in the preferential debts of the estate were introduced by the 1997 amendment of the Bankruptcy Act,<sup>455</sup> the original regulations are, in essence, reinstated in the BRL. Pursuant to new regulations in Art. 336, 345 et seq. BRL, the proceeds of the sale of secured debtor's assets are not included in the insolvency estate fund, but are - after deduction of the cost of realisation - transferred to the respective secured creditors up to the amount of their claims. However, Art. 346 BRL stipulates that the proceeds of sale of real estate, of usufruct in connection with inheritance, of sea ships registered in the ship register and of cooperative rights on housing space are distributed between secured creditors only after certain privileged claims (alimony, salaries of employees for the last three months, some pension claims) have been satisfied. Creditors whose claims are secured by registered pledge can be satisfied – if the pledge agreement includes such clause – by taking over the pledged object or by selling it outside the execution proceedings according to Art. 314, 327 et seq., 333 BRL.<sup>456</sup>

Different ranks of claims introduced by the 1997 amendment to the Bankruptcy Act as a compensation for the loss of the right to a separate satisfaction of claims have been deleted; instead of ten ranks under previous law, there are only four claim ranks under the BRL (Art. 342

<sup>455</sup> For details see A. Jakubecki, Satisfaction of secured creditors after opening of the bankruptcy proceedings as regulated by the new provisions of the Bankruptcy Act, *Przegląd Sądowy* 1998, no. 2 (in Polish).

<sup>456</sup> See P. Janda „The Satisfaction of a Creditor secured by registered Chattel Mortgage in Insolvency Proceedings with the aim of Liquidation“ (in Polish), *Monitor Prawniczy* 17/2005, p. 841 et seq.

BRL). Privileged claims such as the expenses of the insolvency proceedings and expenses in connection with debtor's assets, salary claims, claims on alimony and pensions payments, claims concerning social welfare contributions, claims of the administrator or trustee on remuneration as well as claims arising from obligations which were accepted by the court supervisor belong to class 1. Claims concerning social welfare contributions for the last year, which are not included in class 1, tax claims and other public claims will rank second. In class 3, all remaining claims with interest are included, exempting those belonging to class 4 (e.g. court or administrative fines, claims on the basis of gift or of legacy).

### **f) Realisation of Debtor's Property**

Liquidation of debtor's assets is carried out generally by selling the movable and immovable assets, by collecting or selling claims of the debtor and by realizing other rights related to the debtor's assets (Art. 306 et seq. BRL).

The administrator is obliged to try to sell the debtor's business as one unit or as several functioning business units. The administration of assets is extended to the continuation of the debtor's business or its lease, if it is possible to conclude an composition or to sell the business at a later time at a higher price. The scheme often used in practice of temporary leasing of the business with an option of purchase is now regulated by law in Art. 316 BRL. Upon the sale of the business as one unit, the purchaser does not assume the liabilities of the debtor according to Art. 317 BRL as opposed to Art. 526 of the Civil Code; he purchases the business free of encumbrances.<sup>457</sup>

If the sale of the debtor's business as one or several functioning units is not possible, then each asset should be publicly auctioned by the administrator under supervision of the judge-commissioner. If assets are not sold at a public auction or the judge-commissioner does not accept

<sup>457</sup> The exemption from liability is applicable also to mortgage, pledge, registered pledge and registration in the ship register which was already stated in the 1997 amendment to the Bankruptcy Act.

the offer, the judge-commissioner can order a second auction or determine the minimum price and conditions of sale and allow the administrator to find a purchaser or allow the administrator to sell assets free of procedural restrictions. The sale of real estate and ships free of procedural restrictions must be approved by the creditors' committee. In this case a company consisting of at least half of the debtor's enterprise's employees and being a commercial company with participation of the Treasury has a pre-emptive right of purchase of the enterprise or functioning enterprise units (Art. 324 BRL).

The sale of movable property free of procedural restrictions must be approved by the judge-commissioner according to Art. 326 et seq. BRL.<sup>458</sup>

### **g) International Insolvency Law**

Neither the Bankruptcy Act nor the Composition Act contained special regulations on international insolvency law; according to the prevailing opinion the territorial principle was to be applied.<sup>459</sup> The decisions of foreign authorities following the opening of the insolvency or composition proceedings abroad could be not enforced.<sup>460</sup> The lawmaker abandoned this solution and adopted new regulations based on the UNCITRAL model of 1997 whereby new provisions are only to be applied if international treaties are not applicable (Art. 378 BRL). After

<sup>458</sup> Ordinance of the Ministry of Justice from 16 April 1998, Dz. U. no. 55, pos. 360, entered into force on 14 May 1998.

<sup>459</sup> See also D. Pawlyszcze, Bankruptcy from the perspective of the provisions of the Civil Procedure Code regarding the international civil procedure and the private international law, *Przegląd Prawa Handlowego*, June 1995, p. 7 et seq. (in Polish).

<sup>460</sup> See F. Zedler, The Bankruptcy Act and Composition Act in Poland, lecture. For general information on the possibility of enforcing other German writs of execution in Poland U. W. Schulze, Country report Poland, in: H. Müller, G.-S. Hök, U. W. Schulze (eds.), *German writs of execution abroad* (in German).

Poland became member state of the European Union in 2004, Art. 378-417 BRL are only relevant for proceedings in which enterprises from non-EU states participate.<sup>461</sup>

With regard to the international references of the insolvency law, the question arises what effects an insolvency proceeding in one state has on a concurrent execution or insolvency proceeding carried out in another state.<sup>462</sup> For the purposes of mutual recognition of foreign insolvency proceedings, the new regulation of Art. 379 et seq. BRL differentiates between main and territorial proceedings. The recognition of foreign proceedings does not prevent the opening of proceedings in Poland, but the Polish proceedings will be secondary proceedings with the aim of liquidation of debtor's assets located in Poland, if the foreign proceedings are main proceedings (Art. 405 et seq. BRL). According to Art. 382 BRL, exclusive jurisdiction of Polish courts is determined if the main office of the debtor's business is in Poland. In other cases, concurrent jurisdiction is determined. Stipulation of jurisdiction by contract is not valid.

The proceedings for recognition is to be commenced upon application of the foreign administrator submitted to the Polish court with the appropriate local jurisdiction. If the Polish court recognises the foreign proceedings, the foreign administrator is allowed to exercise his functions in Poland concerning administration and liquidation of debtor's assets under supervision of the Polish court (Art. 401 BRL). The court and the judge-commissioner co-operate with foreign courts or administrators directly, Polish administrators, court supervisors or trustees co-operate via the judge-commissioner (Art. 413 et seq. BRL).

<sup>461</sup> See Regulation of the European Council 1346/2000 from 29 May 2000, entered into force on 31 May 2002.

<sup>462</sup> See also J. Brol, On the international aspects of bankruptcy and bankruptcy proceedings, *Przegląd Prawa Handlowego* December 1998, p. 8 et seq. (in Polish).

## **h) Criminal Offences in Connection with Bankruptcy**

Poland introduced with the Law on the Protection of Business Transactions, entered into force on 31 December 1994,<sup>463</sup> a system of sanctions for criminal offences in connection with bankruptcy. The criminal offences defined by Art. 6-10 of the Law were inserted nearly unchanged into the new Polish Penal Code, in Art. 36 “Criminal offences related to business transactions”.<sup>464</sup> The criminal offences concerning bankruptcy<sup>465</sup> as well as the favouring of creditors and debtors are similar to those provided by the German Federal Penal Code, additionally, the false bankruptcy, i.e. the simulated bankruptcy to intentionally defeat the creditors, known as “asset stripping” is included. The criminal liability is extended to all persons involved in an insolvency proceeding.

Apart from these provisions, the delayed filing for insolvency by the representatives of executive organs of corporations is deemed as criminal offence under Art. 586 of the Law on Commercial Companies. Additionally, Art. 522 et seq. BRL sanction providing of wrong or insufficient information about property and financial situation by the debtor before and after the court decision on opening the insolvency proceedings (also within the preliminary reorganisation).

<sup>463</sup> Dz. U. 1994, no. 126, pos. 615 as amended.

<sup>464</sup> After the new Penal Code (Dz. U. 1998, no. 88, pos. 553) entered into force on 1 September 1998, the Law on the Protection of Business Transactions was repealed.

<sup>465</sup> As under German legislation (§ 283 Para. IV u. V Penal Code) Art. 301 § 3 of the Polish Penal Code embraces negligent bankruptcy; see E. Hryniewicz, R. Zawłocki “Negligent Bankruptcy as a Criminal Offense” (Polish), *Monitor Prawniczy* 6/2006, p. 293 et seq.

## 5. Summary and Perspectives

The long experience of Western Europe with insolvency law, especially when it does reflect issues, which are not of a primary legislative character, e.g. the problem of determining over-indebtedness, is of great value for the transition countries developing their insolvency law. Furthermore, the multitude of court decisions laid down in time like the pieces of a mosaic, have composed an image reflecting as a mirror the insolvency law in all its facets and could be very useful for legislative bodies, judges and insolvency administrators. Since Poland joined the European Union in 2004 and, consequently, will more actively participate in the European process of law unification, European insolvency law will gain importance for Poland. Like Romania and Croatia, Poland followed in its reform of insolvency law the model of the new German Insolvency Law.

Reorganisation models provided by the corporate law, confirmed by the practice in Western Europe, such as restructuring, takeover and rescue company, seem gradually to find more acceptance in Poland. The Polish lawmaker introduced a wide range of restructuring instruments in the BRL, including debt-to-equity swaps, compulsory administration, discharge of residual debts, and sales of claims at market price. If the ambitious preliminary reorganisation proceedings meet the great expectations is not yet clear.<sup>466</sup> Regulations on writing-off of claims and tax regime in case of restructuring and reorganisation are still lacking. Furthermore, instruments outside of insolvency proceedings, such as out of court settlement<sup>467</sup>, arbitration and mediation<sup>468</sup>, which has been

<sup>466</sup> See also a cautious evaluation in the EBRD Legal Indicator Survey: assessing insolvency laws after ten years of transition, Individual country assessments (2003); login: 26.02.04, <http://www.ebrd.com/country/sector/law/index.htm>.

<sup>467</sup> See J. P. Naworski „The out of Court Settlement – chosen Problems“ (in Polish), *Przegląd Prawa Handlowego* April 2005, p. 15 et seq.

<sup>468</sup> Law of 28. July 2005, Dz. U. no. 178, pos. 1478; see K. Falkiewicz, R. L. Kwaśnicki „Arbitration and Mediation in the light of the recent novelisation of the Civil Procedure Code“ (in Polish), *Przegląd Prawa Handlowego* April 2005, p. 15 et seq.

newly introduced into the Civil Procedure Code, are gaining importance.

In order to overcome the difficulties encountered particularly in determining over-indebtedness based on the status of assets and liabilities, an approach similar to the German regulation could be introduced. The German regulation is based on a twofold modality of determination, including (1) the accounting determination of over-indebtedness using the liquidity values and (2) the adjustment of over-indebtedness assessment depending on the liquidity figures if the profit and survival forecasts based on the "going concern" criteria are positive. Apparently, this open concept of over-indebtedness combined with proper public directives would be more suitable to guarantee legal certainty; especially in view of involvement of experts for taking evidence in the phase before opening the proceeding which has been introduced this concept could be successfully implemented. The objective of reducing the duration of proceedings should also not be ignored in the future.