'23 YEARBOOK

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Contents

Dear Readers,

The law traditionally tries to keep up with reality, and then all of us already functioning in the new reality try to keep up with the law. Lawmakers are pressured to regulate everything explicitly. This gives rise to recipes, not regulations. Many issues don't need to be separately regulated at all. It can be enough to appropriately interpret and apply the existing law.

Regulations have finally been adopted in Poland governing remote work—a familiar phenomenon for several years. Will it be easier? The parliament is also trying to bring relief to borrowers—does it have a chance of success?

Inflation at a level unwitnessed for decades is sowing mayhem. How to cope when increases in prices of materials and energy render existing contracts unfeasible? How to pursue the long-planned energy transformation in a way that can also help slow inflation?

And it is high time for decisive measures across many other areas. At a time of crisis in markets for raw materials, we cannot afford to thoughtlessly discard packaging. A planned deposit system is supposed to prevent this. It is also time to stop turning a blind eye to environmental and human rights issues along other links of global supply chains. Here the proposed Corporate Sustainability Due Diligence Directive should help us see more clearly.

Sustainability is now a mainstream concept across the board, and shapes various aspects of business operations. We write about this from the perspective of M&A, competition, and essential internal procedures.

In the 2015 *Yearbook* we reported on a new phenomenon, the Internet of Things. Now, in 2023, we write about the Internet of Bodies, which is not all that new but in regulatory terms still leaves a lot of ground to cover. And from a regulatory point of view (and more specifically under employment law) we raise the issue of the metaverse.

While discussing the need for regulation, we should not forget that on many issues we can manage quite well using the old legal system, even in areas opened up by new technologies.

Beyond this, how to prepare for implementation of new regulations on whistleblowers? Can shareholders or partners compete with their own company or partnership? How can manufacturers of drugs, medical devices and dietary supplements advertise in Poland? And a few more topics.

We invite you to read our new *Yearbook*.

The Editors

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Remote work: New regulations for working away from work

Starting in April 2023, new regulations governing work away from the employer's location will take effect in Poland. Provisions on "remote work" will replace the old regulations on "telework." What responsibilities do the new provisions entail, and how will remote work differ from telework?

Both telework (*telepraca*) and remote work (*praca zdalna*) allow the performance of work away from the employer's location. Under the new regulations entering into force on 7 April 2023—Art. 67^{18}–67^{34} of the Polish Labour Code—in the case of remote work, employees will be entrusted with the initiative to indicate where they will perform their duties. This is reflected in the definition of remote work, which shows that while the location of remote work should be agreed by the parties to the employment contract, it is the employee who should propose the location.

The concept of remote work

Unlike telework, remote work does not require the employee to communicate with the employer via electronic communications. Unlike telework, certain activities cannot be performed as part of remote work, specifically:

- Particularly dangerous work
- Work causing permissible physical parameters for living quarters to be exceeded
- Work with hazardous chemical agents
- Work associated with the use or release of harmful biological agents, radioactive substances, or any substances emitting offensive odours
- Work generating lots of dirt.

Remote work is seen as a convenience for the employee, and for this reason the employer must agree to remote work by certain people. This right has been given to persons caring for a family member. The employer will be able to reject their request for remote work only if it is impossible due to the organisation of the work or the type of work performed by the employee. The new regulations do not define this notion, but examples of circumstances that an employer might cite when arguing against remote work include:

- Significant financial costs associated with this form of work
- Impossibility of effective teamwork
- The need to use devices located in the employer's office
- Inability to ensure confidentiality of information provided by the employee.

Introduction and termination of remote work

Like telework, remote work requires an agreement with the employee. Such arrangements can be made when entering into the employment contract or during the course of the employment relationship.

An interesting new feature is the ability to order an employee to work remotely. This possibility exists during the period of a state of emergency, a state of threat of an epidemic, or state of epidemic, and for three months after such state is called off. Also, the employer may issue such an order if it is not otherwise possible to provide safe and sanitary conditions due to *force majeure*.

For the employer to require compliance with such an order, the employee must make a declaration that he or she has the premises and technical conditions for performing remote work. However, the new provisions do not introduce any possibility to check whether an employee who asserts a lack of adequate premises and conditions is telling the truth. Thus employees who don't want to work remotely might easily avoid it. On the other hand, an employer who succeeds in establishing that an employee has lied can take action against the employee, not excluding disciplinary termination.

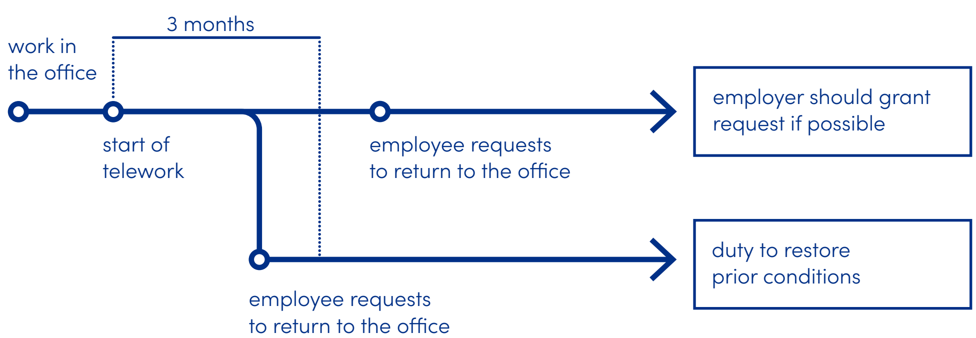
A significant difference from the regulations on telework is the fairly flexible method of introducing remote work during the employment relationship. In this regard, the arrangements do not have to be in the form of a written agreement amending the employment contract. Therefore, remote work can be arranged by the employer and employee verbally or by email.

Under the old provisions, if telework was introduced during the course of the employment relationship, the employee had three months to apply for a return to work in the office. The employer had to accept such a request. If the request was made later, the employer could grant or deny the request (but was supposed to grant the request if possible).

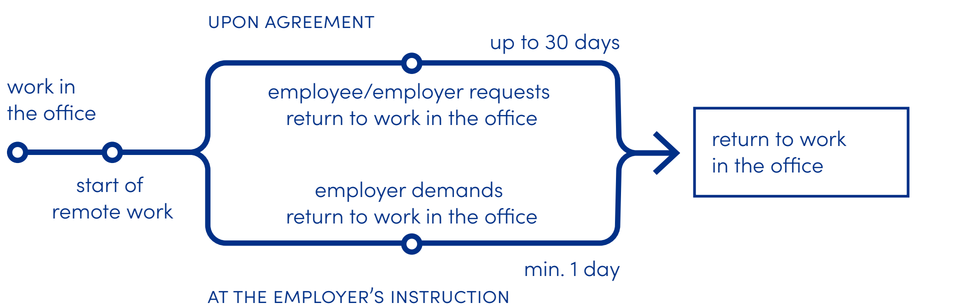
In the case of remote work, either party may request reinstatement of the previous working conditions at any time. This shall take place within the period agreed by the parties, not more than 30 days after receipt of the request, and in the absence of agreement, 30 days after the request was delivered to the other party. The request can be submitted in written or electronic form and does not require justification.

It should be pointed out that if remote work begins as a result of an order from the employer, the employer may require the employee to return to the office at any time, while ensuring that the employee is given at least one day to appear at the workplace.

TELEWORK



REMOTE WORK



Form of determining the rules of remote work

The regulations for establishing the rules for performance of work outside the office are similar for telework and remote work. These rules can be established by agreement with trade unions, in workplace rules issued by the employer, or in an agreement between the employee and the employer. Additionally, in cases where remote work is performed at the employer's order, the rules for performing remote work may also be specified by order of the employer.

Pursuant to Art. 67^{20} §6 of the Labour Code, these documents should define issues such as:
– The group or groups of employees who may be subject to remote work
– Rules for the employer's coverage of costs associated with remote work
– Rules for oversight of the performance of remote work
– Safety rules
– Data security and protection rules.

Oversight of performance of work at home

The scope of oversight of telework and remote work is similar. An important difference is the possibility for the employer to inspect the place of remote work also in order to verify whether the procedures protecting the confidentiality of business information held by the employer are maintained. This additional area of oversight was introduced following alarms raised by employers pointing out the risk of disclosure of trade secrets in the course of remote work. In this respect, if deficiencies are found, the employer can withdraw consent to perform remote work.

Notably, as in the case of telework, conducting an inspection of remote work must be agreed with the employee.

	TELEWORK	REMOTE WORK
Definition	Work that can be performed **regularly outside the workplace** using means of electronic communications (within the meaning of the regulations on electronic services)	Work that may be performed **wholly or in part at a place designated by the employee** and agreed upon in each case with the employer, including at the employee's home, in particular using means of direct remote communication
Who always has the right to work outside the office?	No one has the right to telework	• Employee who is the parent of a disabled child • Pregnant employee • Employee raising a child up to age 10
Where are the specific conditions for performing work outside the office defined?	• Agreement with the workplace trade union organisation • Workplace rules • Agreement with the employee	• Agreement with the workplace trade union organisation • Workplace rules • Agreement with the employee • Employer's order
Scope of oversight in the employee's home	• Performance of telework by the employee • Installation, inventory, maintenance, service or repair of equipment entrusted to the employee • Occupational health and safety	• Performance of remote work by the employee • Compliance with health and safety regulations • Compliance with security and data protection requirements
Opportunity for occasional work	No, but informal home office work often used	Yes
Employer's occupational health and safety obligations do not include:	• Construction and modification of buildings • Ensuring the safe and hygienic condition of working premises • Provision of adequate hygiene and sanitation devices	• Organisation of the workplace • Provision of meals and refreshments • Provision of sanitary devices and essential personal hygiene products

The employer is also not required to reimburse employees for expenses they incur due to occasional performance of remote work.

Occasional work

The new regulations take account of the frequent practice in which employees requested to be allowed to work in a home office from time to time. Since such work was irregular in nature, the telework provisions did not apply to it, and there were no provisions specifying the rules for performing such work (e.g. as to compliance with occupational health and safety regulations).

In the case of remote work, it is permissible to perform such work occasionally, up to 24 days a year. In that case, it is not necessary to specify the rules for performing remote work in workplace rules or in an agreement. The employer is also not required to reimburse employees for expenses they incur due to occasional performance of remote work.

Occupational health and safety obligations for remote work

One of the significant changes introduced by the remote work regulations is the reduction of the employer's obligations regarding safe and healthy working conditions. First of all, the duty to organise the workstation in accordance with regulations and ergonomic principles was shifted to the employee. This means that it is up to employees working remotely to ensure that they have a properly positioned desk and a chair that meets the requirements imposed by law.

Summary

The new regulations on remote work draw on the experience of using telework and work from home in Poland during the period when Covid regulations were in force. While the parliament has not managed to avoid a number of ambiguities, the new regulations are more responsive than the old ones to the needs of both employees and employers. As working from home becomes a permanent fixture in the realities of labour relations, hopefully the new regulations will make it possible to organise the performance of work more effectively. But it is too early to reach a final assessment.

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From WIBOR to WIRON: The perspective of banks and borrowers

Over the past several months, inflation has skyrocketed in Poland, and with it interest rates. The main reference rate for debt instruments denominated in Polish zloty, the three-month WIBOR (Warsaw Interbank Offered Rate), rose from 0.21% in July 2021 to 7.61% in early November 2022. This results in serious difficulties for holders of variable-rate PLN loans. One of the answers to that problem is supposed to be a reform of the benchmark rate used in Poland, namely WIBOR. Can it succeed?

Recently, holders of residential mortgage loans in Polish zloty have found themselves in a tough spot. Their mortgage instalments have sometimes increased dramatically, and for some borrowers are already about double what they were just a year ago.

This situation is exacerbated by the fact that the vast majority of residential mortgage loans issued in Polish zlotys are variable-rate loans, which distinguishes Poland from many other European countries, where fixed-rate residential loans are standard and consequently borrowers are not affected by interest-rate fluctuations.

To the borrowers' rescue

The plight of mortgage borrowers with loans in Polish zlotys has prompted the Polish government to take steps to come to their aid. In addition to a loan repayment holiday, one of the government's ideas was to reform the WIBOR reference rate, or even to stop calculating it altogether and replace it with another rate. In April 2022, during the European Economic Congress in Katowice, Prime Minister Mateusz Morawiecki announced a plan to help borrowers, consisting of four pillars. One was to replace WIBOR with an alternative, more transparent reference rate, based on the rates used for wholesale overnight deposits. In theory, and according to government declarations, this was supposed to reduce the interest paid on floating-rate debt in Polish zlotys, currently based on WIBOR, since the new benchmark was supposed to be lower than WIBOR. It has been argued that the recently quoted WIBOR levels are excessive and unfair, and the method for calculating them is unclear and prone to manipulation.

BENCHMARK REGULATION

- EU Regulation on indices used as benchmarks in financial instruments and financial contracts
- Strictly regulates the administration of benchmarks
- Classifies WIBOR as a "critical" benchmark, meaning that it is subject to especially rigorous regulation

WIRON (WARSAW INTEREST RATE OVERNIGHT)

- Risk-free rate (RFR)
- Retrospective—concerns past periods (specifically the previous day)
- Based on rates applied in actual transactions on the wholesale overnight deposits market

RFR-type rates are regarded as more transparent, more representative of the market they are designed to measure, and less susceptible to manipulation.

Some members of the ruling camp even suggested that the new rate could replace WIBOR only in residential loans, while WIBOR would continue to be calculated and used for example in corporate loans or bonds.

Confrontation with the requirements of the Benchmark Regulation

However, these initial ideas and proposals did not seem to fully take into consideration that the calculation and use of benchmarks, as well as possible replacement of WIBOR, are strictly regulated by the EU's Benchmark Regulation (2016/1011, also known as the BMR) on indices used as benchmarks in financial instruments and financial contracts. What is more, WIBOR is a "critical benchmark" within the meaning of the BMR, which makes it subject to particularly stringent regulation.

In practice, mainly, this means that lawmakers, the Minister of Finance, and financial regulators cannot replace WIBOR with an alternative rate only in certain categories of contracts, e.g. residential mortgage loans, while at the same time maintaining WIBOR in other types of contracts. According to the BMR, when a critical benchmark is replaced, it is replaced in principle, by operation of law, by the designated replacement benchmark in all contracts in which the replaced benchmark appears, unless the contracts contain a fallback clause meeting the requirements for a "suitable fallback provision" described in the BMR and indicating another replacement benchmark in the event that calculation of the replacement benchmark ceases. What is more, the replacement procedure set forth in the BMR requires that on the date of replacement of the reference benchmark, calculation and publication of the replaced benchmark has to cease completely.

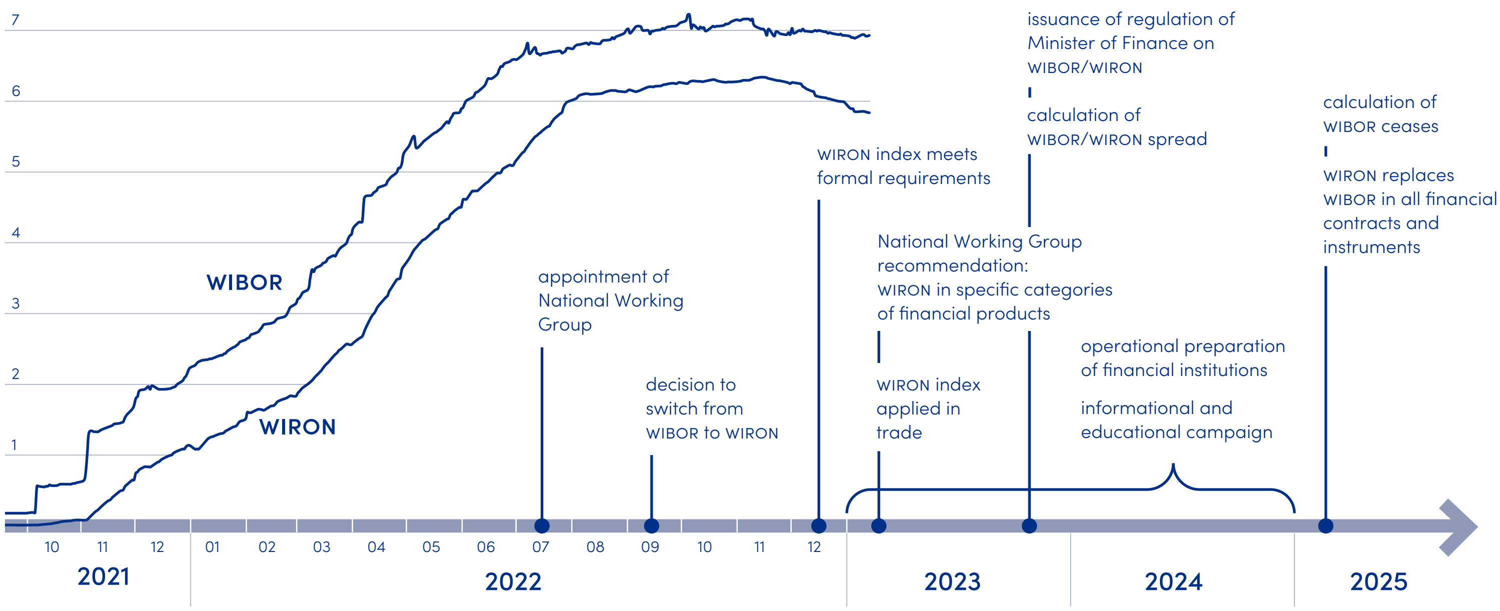
Replacement of the WIBOR rate will affect not only natural persons holding residential mortgage loans, but the vast majority of debtors and creditors under borrowings on which a variable interest rate is charged.

As a consequence, considering the requirements of the BMR, replacement of the WIBOR rate will affect not only natural persons holding residential mortgage loans, but the vast majority of debtors and creditors under borrowings on which a variable interest rate based on WIBOR is charged, including debt under corporate loans, bonds, intercompany loans, bank loans, and other popular financial products such as leasing and factoring.

Will the reform bring relief to borrowers?

Therefore, the question arises what exactly this impact will be. Will replacing WIBOR with a new benchmark rate upset the economic balance between lenders and borrowers? It would seem that this should be the case, given that the WIBOR reform was initially presented as a method to ease the burden of rising mortgage instalments on borrowers. But in principle, replacement of benchmarks under the BMR is not intended to alter the economic equilibrium between debtors and creditors from what they agreed in their financial documentation.

What is more, the standard practice in replacing benchmarks, including pursuant to the BMR, is to apply a spread adjustment in any case where a simple substitution of one benchmark for another would lead to



distortion of the economic parameters of the contract agreed by the parties. Usually, the spread adjustment is calculated as the median of the daily difference between the old and new rates, calculated over a five-year retrospective period for each day on which both rates were calculated during that five-year period.

In other words, replacing WIBOR with a new benchmark in the manner set forth in the BMR would actually affect almost everyone who has any type of contract referring to WIBOR. But so far nothing suggests that borrowers will soon be paying less interest thanks to such a change, benefitting from an administratively imposed strengthening of their position.

Further stages of the reform

In July 2022, the National Working Group on Benchmark Rate Reform was constituted and entrusted with the task of reforming the benchmark rates in Poland. As the rate that will replace WIBOR, the working group has indicated WIRON (Warsaw Interest Rate Overnight) (formerly known as WIRD), a benchmark calculated based on data from the market for wholesale overnight zloty deposits. Thus, the change will actually follow the worldwide trend of replacing interbank offered rates (IBOR) with risk-free rates (RFR). IBOR rates are rates pertaining to future periods, offered for interbank deposits of a specific duration, e.g. one month, three months, six months, etc. On the other hand, as a rule, RFR rates are retrospective rates, thus pertaining to past periods (specifically the last 24 hours), usually based on rates used in actual transactions in the wholesale overnight deposit market. In general, RFR rates are considered more transparent, more representative of the market they are supposed to measure, and less susceptible to manipulation.

Also, the working group indicated that the switch from WIBOR to WIRON will involve an adjustment of the spread, calculated in the standard manner described above, i.e. as the median of the daily difference between the value of the benchmark being swapped and the value of the new benchmark, calculated for each day in the five-year lookback period for which the two benchmarks were calculated. In other words, in the meantime, unless other protective measures are adopted in favour of borrowers, the spread adjustment will leave the economic balance between debtors and creditors essentially unshaken, and borrowers are unlikely to experience relief due to a reduction of principal and interest instalments below what they would have been if WIBOR were still in effect.

The date when all references to WIBOR in existing contracts will be replaced by WIRON by operation of law is likely to be 1 January 2025. However, banks will be encouraged by the Polish Financial Supervisory Authority to start applying WIRON in new contracts as early as 2023.

Both banks and their customers will need to prepare for this, especially since the methodology for calculating the interest on a loan or other debt instrument using WIRON (a retrospective benchmark based on overnight transactions) will be significantly different from how the interest is calculated based on a traditional forward rate on future periods of a certain duration, such as WIBOR. This difference will have to be reflected in the wording of contracts for financial products.

In some contracts with fallback clauses, the replacement rate will in fact not be WIRON, but another rate, indicated by the fallback clause applied in the contract in question.

The key role of fallback clauses

Banks and their clients will also need to consider and analyse any fallback clauses in their existing and new financial contracts. Fallback clauses in financial contracts are intended to indicate a replacement benchmark in the event that an existing benchmark specified in the contract ceases to be calculated and published. If a fallback clause meets certain requirements set forth in the BMR, it may ensure that the benchmark replacement that would otherwise have occurred by operation of law under the BMR in the absence of such a clause will not occur for that contract, and instead the previous benchmark will be replaced by another benchmark indicated in the fallback clause. In other words, if in 2025, by operation of law, WIBOR is replaced by WIRON in compliance with the BMR, it is possible that in some contracts with fallback clauses, the replacement rate will in fact not be WIRON, but another rate, indicated by the fallback clause applied in the contract in question.

Therefore, for market participants to properly understand their legal and financial situation in connection with the discontinuation of WIBOR, they will need to take a closer look at their existing financial contracts, including any fallback clauses they contain. They will also need to understand how to interpret and possibly negotiate fallback clauses in new financial contracts.

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Judicial intervention in the terms of contracts

Regardless of their field or scale of operations, many businesses are struggling with the problem of rapid rises in prices of natural gas and electricity. The increases may be so great that contracts concluded in the past may cease to be profitable to perform, but instead generate heavy losses. Similar problems are sparked by increases in prices of other commodities (such as steel or aluminium), chiefly impacting the construction market. In such situations, can the contractor refuse to perform?

In a stable economy, contracts for supply of goods have often been concluded for several years at a time, without any price adjustment mechanisms. But construction contracts are by their nature long-term contracts. What to do if prices of materials, electricity or gas have risen so strongly since the time when the contract was concluded that performance of the contract could generate huge losses for the contractor, or even threaten its economic situation?

The Polish Civil Code provides a special solution for this situation, the change-of-circumstances clause, also known as *rebus sic stantibus* (Art. 357^{1}). Based on this provision, courts can issue judgments offering an opportunity to adjust the terms of contracts concluded in the past to suit the current market situation, or to immediately halt performance of the contract.

Market changes and the situation of businesses

Everyone is closely tracking evolving market conditions, including significant increases in prices of materials (particularly building materials), natural gas and electricity. The rapid changes are impacting both households and industry. In this situation, many counterparties maintain a loyal attitude and voluntarily agree to increases in contract prices to reflect current market conditions. They understand that the rising prices are caused by external factors, and the related risk should be shared to some extent. After all, the current market trends are extraordinary and are not the sort reflected in normal business cycles.

Many businesses wonder whether they can compulsorily (through the courts) modify contracts concluded in the past that did not foresee the risk of drastic price increases.

Rebus sic stantibus clause

Many businesses wonder whether they can compulsorily (through the courts) modify contracts concluded in the past that did not foresee the risk of such drastic price increases. If the other party is not inclined to cooperate, they must seek solutions other than negotiations and amicable resolution of the issue. Lawmakers in Poland have anticipated and regulated such situations. The principle of the enforceability of contracts (*pacta sunt servanda*) prevails in civil law, but it is not absolute. The change-of-circumstances (*rebus sic stantibus*) clause (Civil Code Art. 357^1) looks beyond this rule and enshrines the right of either party to a contract to pursue a claim before the court to modify or even dissolve the contract.

The aim of this institution is to ensure flexibility in the terms of contracts and the possibility of adjusting them post-signing to reflect the evolving commercial and economic situation. The *rebus sic stantibus* clause rejects the grossly unjust and sometimes irrational consequences of strict compliance with the principle of the enforceability of contracts. Civil Code Art. 357^1 thus protects the interests of the parties to a contract against negative changes in social relations throughout the performance of the contract. This is particularly relevant in the case of long-term contracts, where performance is spread out in time. This institution provides judicial protection to entities impacted by economic change, restores the contractual equilibrium between the parties, and allows economic risks to be redistributed more equally.

The code sets forth four conditions for applying this institution under Art. 357^1:

- An extraordinary change in circumstances
- Excessive difficulty or the threat of a gross loss for one of the parties if it performs as provided under the contract
- A causal connection between the extraordinary change in circumstances and the excessive difficulty or threat of a gross loss for one of the parties
- The unforeseeability by the parties to the contract of the impact of the extraordinary change in circumstances on performance of the contract.

Extraordinary change in circumstances

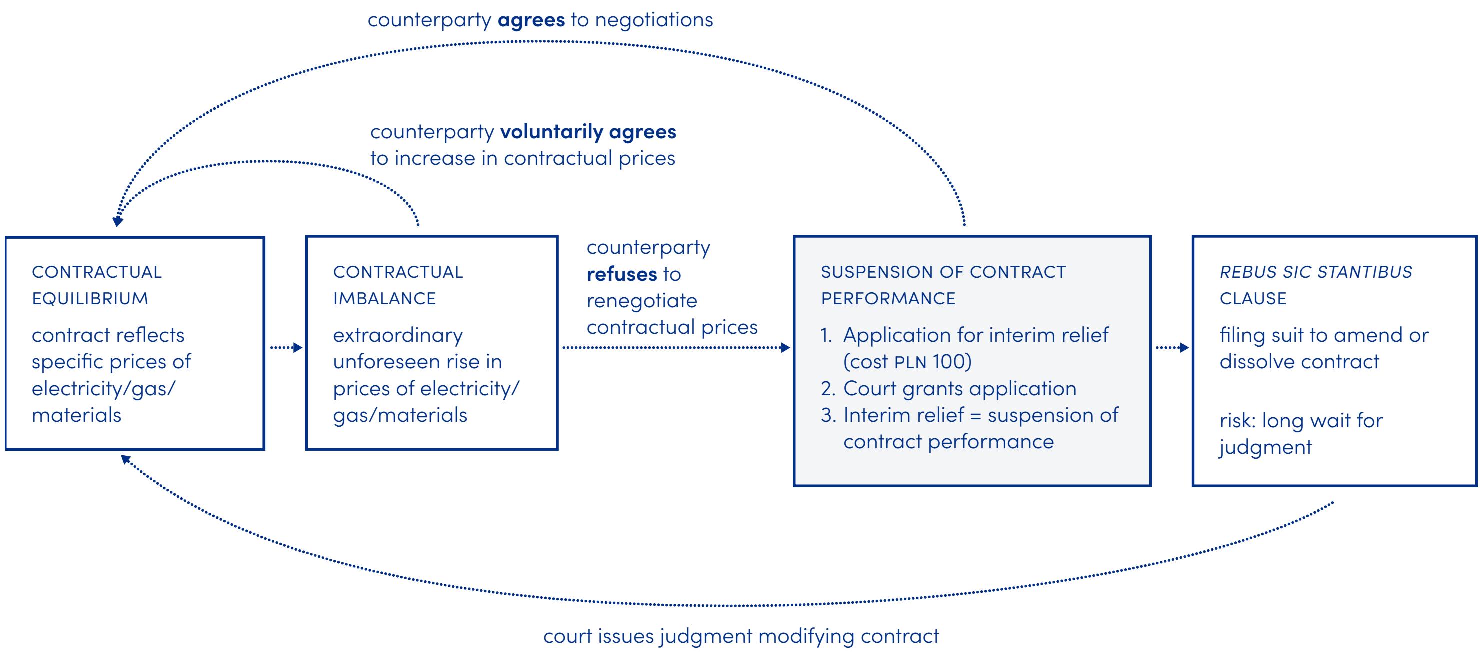
The change in circumstances must be general in nature, universal, not affecting only the parties to the specific contract. The extraordinary nature of the change means that it is exceptional and not to be encountered in the ordinary course of business. The change must also extend beyond the ordinary contractual risks which professionals assume in their contracts. Moreover, it must not have been possible for the parties to foresee the impact of the extraordinary change in circumstances on completion of the agreed performance. Thus this does not refer to changes of an individual nature, but rather to universal market trends affecting the overall set of entities operating in a given market. The change must be external and beyond the parties' control.

In assessing whether the change is extraordinary, the court will examine first and foremost the arguments raised by the parties related to the current market situation, and compare that situation to the situation in which the parties concluded the contract. If at the contracting stage they could have foreseen the change, the institution of *rebus sic stantibus* will not be applicable. Thus it would be questionable to rely on a change in circumstances if the parties concluded the contract after the Covid-19 pandemic or the war in Ukraine had already broken out. A party asserting claims under Civil Code Art. 357^1 must show that the specific consequences of these events were not yet known or foreseeable at the time of concluding the contract. In the case of the pandemic this should be easier, as it evolved over time and the various economic phenomena related to the pandemic arose after the fact, and not all at once. At the start of the pandemic it was hard to predict the exact consequences for global markets or the scale of changes just beginning to occur.

The Covid-19 pandemic and the war in Ukraine

The Covid-19 pandemic and the war in Ukraine may constitute an extraordinary change in circumstances within the meaning of Civil Code Art. 357^1. The impact of the Covid-19 pandemic, but even more so Russia's launch of a war on the territory of »

The *rebus sic stantibus* clause protects the interests of the parties to a contract against negative changes in social relations throughout the performance of the contract.



a neighbouring sovereign state, seriously shook the economic stability of the electricity and gas markets. It is common knowledge that Russia is a global leader in the supply of natural gas, and its operations on this market have a major impact on prices. Abandonment of the Nord Stream 2 project and interruptions in the delivery of gas by the Nord Stream 1 pipeline are generating unusually serious consequences for the accessibility and prices of natural gas, driving up the price. As coal producers, Russia and Ukraine also exert an impact on accessibility of coal in Poland, which in turn carries over to the ability to use this fuel at coal-fired power plants. In one case, the court held that these circumstances were notorious—universally known—and did not require proof. The court thus took judicial notice of these facts (Civil Procedure Code Art. 228 §1). This holding offers a far-reaching procedural advantage, as it relieves the party of the burden of proving that the changes are extraordinary. Otherwise, the litigant would have to call an expert witness to testify to market trends, the nature of the phenomena occurring on the market, and their impact on the economy. That is a tall order, requiring specialised knowledge and a thorough analysis of the case.

Stay of performance

Such an extraordinary situation opens the possibility to apply the *rebus sic stantibus* clause and seek modification or dissolution of the contract. Before filing suit, the plaintiff has the option of seeking interim relief, for example in the form of suspending performance of the contract. In one case, for example, the court issued an order granting interim relief by halting supplies during a specific period of contract performance. This ruling shows that the courts perceive the difficult market situation and take into consideration its impacts on business operations, particularly manufacturing, which is especially hard-hit by changes in electricity and gas prices. Similar rulings may be expected in the construction industry, strongly impacted by changes in prices of construction materials, putting many contractors in a tough situation, where they have to perform the contract for a fee that does not reflect current market rates.

Interim relief can also offer a strong argument in negotiations by the parties and allow them to reach a faster amicable resolution of the dispute. Halting supplies, or more generally halting contract performance, may incline the other party to make concessions and cover (at least partially) the rising costs of electricity, gas and other materials. The low court fee may offer an additional incentive to seek interim relief in such cases. In a case seeking dissolution of a contract, the fee for filing an application for interim relief is only PLN 100.

A stay of contract performance by the court may lead to a situation in which the other party to the contract will be willing to accept a surcharge on top of the prices agreed in the contract. The surcharge should cover the loss resulting from the increasing prices of electricity and gas. This solution enables restoration of contractual equilibrium to the parties in a very short time, without waiting for years for a judgment on the merits. Otherwise, litigation under the *rebus sic stantibus* clause can be highly complex and time-consuming, and our experience shows that cases can drag out over several years. Meanwhile, the changing market situation requires an immediate response, so that judicial protection does not come too late. This is why it is worth seeking interim relief, to help bring about a fair and amicable resolution to the parties' differences.

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Indexation clauses in public contracts: Do they work?

At a time of rapid growth in prices, an advantage of public procurement contracts is that most of them include indexation clauses, which can adjust the fees to bring them in line with reality under changed circumstances. But some commentators claim that these clauses do not serve their purpose. Is that true? And if so, what is the reason?

Public procurement contracts may be concluded within a special regime, but under Polish law they constitute obligations within the meaning of the Civil Code. In this sense, under Civil Code Art. 358^1 §1, the consideration described in the contract is subject to the rule of "nominalism." This means that if the subject of an obligation from the time the obligation is contracted is a sum of money, fulfilment of the consideration occurs through payment of the nominal sum, unless otherwise provided by specific regulations.

Such specific regulations include those in the Public Procurement Law of 11 September 2019 which allow the amount of the contractual fee to be modified from the amount originally established upon award of the public contract. Art. 439(1) of the Public Procurement Law provides that a contract for construction works, supplies or services concluded for a period of longer than six months must contain provisions for modifying the amount of the fee payable to the contractor in the event of a change in the price of materials or costs connected with performance of the contract.

This wording is a result of changes introduced by the Act of 7 October 2022 Amending Certain Acts to Simplify Administrative Procedures for Citizens and Businesses. Until entry into force of this special act (and in light of the transitional provisions), this provision did not cover supplies, and otherwise applied to contracts concluded for a period of longer than 12 months.

Although this is not the only provision of the Public Procurement Law describing conditions for modifying the fee of a contractor under a public contract, Art. 439 is most closely associated with indexation.

Indexation is a modification of a public contract

Indexation is a specific form of modification of a public contract. Nonetheless, the contractual provisions must be framed in compliance with Public Procurement Law Art. 455(1)(1), which describes the general rules for modifying a public contract without conducting a new tender procedure. In practice this means that the grounds for modifying a contract (including indexation terms) proposed by the contracting authority in the draft contract must be clear, precise and unequivocal (regardless of the value of the modification), and the specific terms on introducing changes in the price must meet the following conditions:

- They must state the scope and nature of possible modifications
- They must state the conditions for introducing modifications
- They cannot provide for modifications that would alter the overall nature of the contract.

The grounds for modifying a public contract indicated in the contract essentially arise out of the contracting authority's predictions of the risk of occurrence of future events that could require a modification. The scope and circumstances under which modifications will be permissible, and when they will not be permissible, depend on the contracting authority's projections. The contracting authority may also decide that a circumstance it has stated will be grounds for modifying the contract, but not fully, only for example within a certain time or up to a certain amount. These forecasts are equally important in the case of indexation clauses, although in this respect there are more restrictions and guideposts in the law.

A contract for construction works, supplies or services concluded for a period of longer than six months must contain provisions for modifying the amount of the fee.

Firstly, under Art. 439(1), the contracting authority is required to include rules in a contract for construction works, supplies or services for introducing changes in the amount of the fee payable to the contractor, and to define the scope of such changes. The contracting authority must define:

- The level of the change in prices of materials or costs entitling the parties to demand a modification of the fee
- The starting date for determining the change in fee
- The manner of determining the change in fee, with reference to an index of the change in prices of materials or costs, or indication of some other basis
- The method of determining the impact of changes in the price of materials or costs on the cost of performing the contract and specifying the periods in which the contractor's fee may change
- The maximum value of the change in the fee.

The grounds for modifying a contract proposed by the contracting authority in the draft contract must be clear, precise and unequivocal (regardless of the value of the modification).

Indexation clauses and the conditions of the specific procurement

Therefore, indexation clauses are obligatory in the circumstances indicated in the act, but their wording is left to be determined by the contracting authority. The contracting authority can tailor the wording of the clauses to suit the conditions of the specific procurement, depending on its needs and—hopefully—its experience in awarding contracts for the specific type of services, supplies or construction works.

The contracting authority should carefully decide whether a change in fee will be made:

- With reference to an index of changes in the prices of materials or costs (the act gives the example of an index published by Statistics Poland) or
- On some other basis (the act gives the example of a list of types of materials or costs for which a change in prices would entitle the parties to demand a change in the fee).

The contracting authority is also required to set a moment in time as the starting point for determining for example the price of materials or costs, for the purpose of comparing how they change over time. If the level of the change exceeds the value indicated by the contracting authority (another mandatory element of indexation clauses), the parties will have the right to demand a change in the fee.

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Can indexation reduce the fee presented in the bid?

It should be stressed that the aim of indexation (not only in public procurement) is primarily to maintain the true value of the consideration to be provided, and of the resulting claims, in relation to a rise or fall in the prices of goods and services. This means that the economic equivalent of the claim which the party should receive as a result of the indexation can be either higher or lower than the original amount. A similar conclusion can be drawn from Public Procurement Law Art. 439(4). A change in the price of materials or costs is understood to mean either an increase or a decrease compared to the prices or costs assumed for the purpose of determining the contractor's fee as set forth for example in the bid. This means that indexation of the fee in a public contract can lead (at least in theory) to either an increase or a reduction in the fee. The wording of the law does not provide grounds for concluding that the contracting authority should be fully chargeable with the risk of a change in prices of materials and costs.

This is also confirmed by Art. 48(2)(1) of the amending act of 7 October 2022. This special act addresses, among other things, the legal grounds for modifying public contracts when their original wording did not allow for modification as a result of a substantial change in prices of materials or costs. Under that provision, if the modification of a public contract involves a change in the contractor's fee, the parties shall bear the increased burden of contract performance in agreed proportions.

Indexation and the contractor's economic risks

Moreover, in public procurement procedures, contractors should (in theory) factor the basic risks into the prices they offer, including the risk of changes in prices over time. Thus, to some degree, this is a normal contractual risk assumed by every economic operator. Only beyond a certain level does this cease to fall within the category of basic risk, and then indexation clauses enable this risk to be managed.

By assumption, thanks to indexation clauses, contractors in public procurement can refrain from factoring risks into their bid above and beyond a basic level. Every contracting authority should view indexation clauses from this perspective. A well-constructed indexation clause should discourage potential contractors from inflating their prices solely to hedge against potential price fluctuations, including atypical ones (which, after all, may not occur). In this instance, it is ultimately the public entity that will pay for the risks factored into the price by the winning contractor. If the contractor could be sure that these risks are mitigated by an effective indexation clause, that would measurably benefit both parties to the contract.

It should thus be concluded that Art. 439 of the Public Procurement Law offers a useful tool, but whether it is properly used in practice depends largely on the contracting authority. After all, it often happens that indexation clauses are merely illusory. This has to do with situations where the provisions of a public contract create an appearance of covering the mandatory area of indexation, theoretically allowing a change in fees to be sought, or even allowing for an automatic change in fees, but the clause cannot be applied in practice or results in an adjustment in the fee that does not reflect the true level of changes (e.g. a change in the purchasing power of money). This may happen for example when the index used is not relevant to the subject of the contract (in particular the main drivers of prices) or the maximum level of changes is too low.

The wording of the law does not provide grounds for concluding that the contracting authority should be fully chargeable with the risk of a change in prices of materials and costs.

Discretion in wording indexation clauses, and their statutory aim

Under Civil Code Art. 353^{1}, the parties entering into a contract may frame their legal relationship within their discretion, so long as the substance or aim does not contradict the nature of the relationship, law, or public policy. It is for this reason, among others, that Public Procurement Law Art. 439 gives the contracting authority discretion to frame the clauses in a public contract in a manner meeting the contracting authority's needs. On the other hand, indexation clauses should reflect that under Civil Code Art. 358^{1} §2, the amount of monetary consideration may be determined according to a measure of value other than money so that the consideration provided by each the parties remains equivalent (Civil Code Art. 487 §2). It follows that indexation clauses are designed so that the two parties to a contract can agree on their mutual obligations in such a way that the consideration provided by each party corresponds (is equivalent) to the consideration provided by the other party.

The National Appeal Chamber's view of indexation clauses

Therefore, it is not the aim of Public Procurement Law Art. 439 to include indexation clauses in public contracts with any and all possible wording. The indexation clause should reflect the totality of the legal rules in this respect. Unfortunately, for a long time this conclusion was not reflected in the rulings from the National Appeal Chamber. Indeed, the chamber held that it was not authorised to examine indexation clauses for their effectiveness and adequacy (for their intended purpose), but was only allowed to assess whether in drafting the clause, the contracting authority included the elements required by the Public Procurement Law (Art. 505(1)). In other words, whether indexation was aimed at actual balancing of the consideration provided by the parties remained beyond the scope of review by the National Appeal Chamber, which often led to upholding the validity of illusory indexation clauses.

It appears that it was finally the economic crisis and the dynamic market situation caused by, among other factors, the war in Ukraine and its consequences, that finally broke through this insupportable line of decisions by the National Appeal Chamber. Today the chamber more and more often takes such steps as increasing the limit of the combined maximum value of changes in the contractor's fee originally permitted by the contracting authority in the draft contract, and also intervenes on the issue of the period after which the first indexation can occur, shortening this period to the contractor's advantage (e.g. in cases KIO 2532/22 and KIO 440/22). For example, the chamber has pointed out in the justifications for its rulings that the originally proposed level of indexation made the indexation illusory in practice, because it did not give the contractor an opportunity to change the fee relative to the actual change in prices of materials or costs associated with performance of the contract. The chamber has also reasoned that to comply with public policy, an increased threshold of the permissible increase in fees should be recognised as warranted.

INDEXATION CLAUSES

Serve their function when:	Don't serve their function when:
Their application causes the consideration of the parties to remain equivalent despite the change in prices or costs	They are poorly worded
They reference an indicator relevant to the subject of the procurement	They are intentionally worded so that they only superficially seem to serve their statutory purpose
Their wording is tailored to the conditions of the specific contract	Their application does not allow the equivalence of the consideration to be maintained in the changing reality of the contract (extraordinary changes in prices or costs)
Their wording reflects the contracting authority's experience awarding contracts for the specific type of service, supply or construction works	They reference an indicator irrelevant to the subject of the procurement
They discourage contractors from factoring atypical risks into the bid price	The maximum allowable change is too low

The point, according to the chamber, is that the economic balance between the parties not be disrupted to the contractor's disadvantage, and also that an excessive increase in the contractor's fee not cause negative consequences for the contracting authority.

Assessment of indexation clauses

So, are indexation clauses in public procurement in Poland a success or a failure? Undoubtedly their use in public contracts should be assessed positively. Objections can be raised primarily to the wording of the clauses in specific contracts, where they sometimes do not suit the type of contract or the main price drivers, or reference indexes that do not effectively bring the fee levels into line with reality.

This problem became more acute during the ongoing economic crisis. The Polish parliament attempted to provide support for all sectors of the public procurement market by amending the Public Procurement Law and introducing additional regulations in the special act of 7 October 2022 cited above. The lawmakers recognised that the Public Procurement Law was not standing up to the test in a time of crisis, and thus the law had to be amended.

But in our view, the source of the problems with indexation clauses is not so much the law as the practice of applying such clauses in contracts. They are sometimes applied unskilfully, or on the contrary, drafted with a full awareness that they will only superficially fulfil the statutory requirements.

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Insurance disputes in the construction industry

In recent years the construction industry has struggled with many challenges, as evidenced by the growing number of disputes in courts and arbitration, also leading to more claims against insurers.

In the post-Covid and wartime reality, construction companies in Poland are facing huge delays in their supply chains, a shortage of workers, and rising costs for transport and materials. The countries currently involved in the war in Ukraine are global suppliers of key materials used in construction, such as copper, aluminium, iron and bitumen. The ongoing war and sanctions imposed on Russia, as well as the significant reduction in Ukrainian exports, are causing difficulties in deliveries and a shortage of building materials.

Under these circumstances, perhaps the greatest challenge for the construction sector is to perform contracts signed earlier at fees calculated prior to the war and the pandemic. Prices of all elements contributing to the total cost of project completion are inexorably rising. Contractors cannot secure timely supplies of materials or the workforce they need. Delays in projects and other types of contractual breaches thus become more and more common. Increasingly, it is also necessary to index construction contracts so that the interests of both the investor and the contractor are duly protected. Nonetheless, we observe that construction projects are often completed at a financial loss, sometimes even exposing participants in the construction process to the danger of insolvency.

Construction dispute = insurance dispute

A large proportion of construction projects for both the public sector and the private sector are secured by performance bonds issued by banks or insurance companies. General contractors and subcontractors are also commonly required to obtain insurance for the duration of the construction process. If the contractor has financial problems—and the

Perhaps the greatest challenge for the construction sector is to perform contracts signed earlier at fees calculated prior to the war and the pandemic.

situation across the sector is tough—contracting authorities or private investors increasingly seek satisfaction of their claims (not always fully justified) by drawing on the established security instruments, and consequently pursue claims against insurers.

Over recent years, construction insurance policies have contained increasingly specialised clauses covering extremely varied types of risks, such as:

- Civil liability insurance for operating in the construction industry
- Contractors plant and machinery (CPM) insurance
- Construction all risks and erection all risks (CAR/EAR) coverage
- Complex coverage for construction employees
- Architects' insurance
- Coverage against transport risks
- Coverage for risks associated with climate change
- Business interruption insurance
- Inherent defects insurance.

The close connection between insurance policies and construction contracts means that whenever claims arise out of a construction contract, insurers will be directly or indirectly involved in the dispute.

Previously it was the investor or contractor who brought the insurer into the dispute, but more and more often the insurer itself decides to actively participate in the dispute from the very start, in order to control and mitigate its exposure to the risk in this area.

As it is harder for construction companies to execute projects based on contracts with a fixed fee, disputes concerning changes in fees—essentially meaning increases in fees—are becoming more numerous, alongside more typical construction disputes (e.g. concerning the difference between "injury" and "defect," or between defects in design and defects in execution). Our experience shows that, unfortunately, in the event of a dispute participants in the construction process are rarely in a position to reach a voluntary understanding. Usually the general contractor (or subcontractor) initiates a claim in court or arbitration against the investor (or general contractor).

This situation could be avoided—or at least the number of disputes of this type could be reduced—if other participants in the construction process, particularly the contract engineer, took a more active and decisive role.

In the case of construction contracts using FIDIC forms (standards published by the International Federation of Consulting Engineers), common in the case of large projects, the contract engineer is authorised to serve as an independent expert determining disputed issues between the investor and the contractor, and in general the contract engineer's determinations are binding. But under the realities of the Polish construction process, the contract engineer essentially becomes part of the investor's personnel, entirely paid by it and defending its interests. This erodes the contract engineer's independence and mandate to determine disputes between the parties.

In the case of disputes under non-FIDIC contracts, the actions of persons whose duty is to control the progress of works and payment for their execution are subject to verification. In this oversight, a contract engineer actively participating in the verification of advancement of the construction process can ensure correct and timely performance of the contract.

In our view, it is in the interest of the insurers for as many disputed issues as possible arising between the parties to construction contracts to be resolved during the course »

ROLE OF THE CONTRACT ENGINEER DEPENDS ON THE TYPE OF CONTRACT

In FIDIC contracts:

- Independent expert and arbiter in investor/contractor relations
- Determinations are generally binding

In non-FIDIC contracts:

- Investor's personnel, paid entirely by the investor
- Protects the investor's interests
- Actively participates in verifying the progress of the project and may ensure correct and timely performance of the construction contract

FIDIC—construction contract forms promulgated by the International Federation of Consulting Engineers (Fédération Internationale des Ingénieurs-Conseils)

It is in the interest of both insurers and insureds to strive for the quickest possible amicable resolution of construction disputes.

of the construction process, without having to resort to litigation. But this requires a willingness by insurers to accept dispute determinations issued on the building site, as well as transparency and impartiality on the part of the entities issuing such determinations. Perhaps these are issues that should be the agreed between the insurer and the party taking out the coverage before issuance of a construction insurance policy or a performance bond.

It should be pointed out by the way that in line with technological development, we are witnessing a significant increase in the number of claims alleging construction defects, as well as claims related to state-of-the-art solutions for example in ecological building (sustainable construction).

Settlement is better than litigation

Rising inflation and costs of implementing construction projects influence the approach to consideration of claims for damages. Disputes lasting for years pose unknowns and risks for both insurer and insured. Insurers must monitor the level of claims and take into account the term and amount of the insurance from the perspective of the condition of the construction industry. If litigation arises, it is worth considering reaching a settlement, which ultimately will mean lower costs.

In our view, it may prove a good solution to establish a joint team of lawyers, insurance brokers, claims adjusters, and construction experts, which can professionally, independently and transparently evaluate the loss and the reasons for its occurrence, and recommend how to cure the loss.

In short, in light of the continuing, hard-to-predict consequences of the pandemic and the war in Ukraine for the construction market, we believe that it is in the interest of both insurers and insureds to strive for the quickest possible amicable resolution of construction disputes. This effect can be achieved by taking more active steps aimed at agreeing the rules for settling such disputes immediately after they arise and accepting the settlements by the parties, including by creating joint expert teams to assess the damage and indicate how to redress it.

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Environmental impact assessment for offshore wind farms

In the Baltic Sea, not a single offshore wind farm has yet to be launched in the Polish exclusive economic zone. This should change soon, as wind farms are essential for achieving the planned energy transformation. A key stage in designing a new wind farm is obtaining an environmental decision, preceded by conducting an environmental impact assessment.

The Polish energy sector is currently in the decarbonisation phase. In recent years the role of offshore wind farms in this process has begun to be recognised, and is consistent with the aims set by the European Green Deal.

The Polish Energy Policy through 2040 was announced in March 2021, describing the long-term strategy for the energy sector and setting the framework for Poland's energy transformation. One of the aims of the policy is the development of renewable energy sources. In light of the anticipated technological development, offshore wind farms should play a special role in achieving this aim.

So far, no wind farms have been put into operation in the Polish exclusive economic zone of the Baltic Sea. According to data from the Supreme Audit Office (NIK), the commencement of construction of wind farms with the shortest timeline for connection to the grid is planned for late 2026 or early 2027, which should enable the first electricity to be delivered to the grid in 2027.

Environmental protection requirements

The Offshore Act (Act on Promotion of the Generation of Electricity in Offshore Wind Farms) was adopted in December 2020. Under Art. 82 of the act, an offshore wind farm and the set of devices for drawing electricity from the facility must meet a range of requirements, including environmental protection. These requirements cover four aspects: design, construction, operation, and closing of the wind farm. The discussion below addresses the first of these aspects.

The prevention principle and the precautionary principle play a key role in the phase leading up to any intervention in the environment, or infringement or impact on the environment. Implementation of offshore wind farm ventures also requires the use of preventive instruments, which include an environmental impact assessment prior to issuance of a decision on environmental conditions for the project.

In the case of operations undertaken in the marine environment, conducting comprehensive analyses based on numerous tests is essential to identify the principal environmental issues, such as:

- Detrimental impact on living marine organisms
- Increased noise levels
- Risk of collisions
- Changes in food chains
- Changes in the benthic habitat (along the sea bottom) and pelagic habitat (through the entire depth of the body of water)
- Pollution due to increased ship traffic.

Decision on environmental conditions for offshore wind farms

Installations in the maritime zones of the Republic of Poland using wind to generate electricity are deemed to be projects likely to have a significant impact on the environment (§2(1)(5) of the Council of Ministers Regulation of 10 September 2019 on Ventures Likely to Have a Significant Impact on the Environment). This means that it is mandatory to obtain a decision on environmental conditions for such ventures (along with the numerous other permits also required to execute a wind farm). The competent body for issuance of a decision is the regional director of environmental protection (RDOŚ) with geographic jurisdiction over the maritime zone along the coast of the relevant province.

The procedure for issuance of a decision is commenced upon filing of an application by the investor or investors involved in executing the venture, along with the enclosures indicated in Art. 74(1) of the Environmental Impact Assessment Act (Act on Access to Information on the Environment and Environmental Protection, Public Participation in Environmental Protection, and Environmental Impact Assessments of 3 October 2008). The most important enclosure, which constitutes a private document with special evidentiary weight, is the report on the environmental impact of the venture. It is subject to verification at a later stage in the proceeding.

The parties to the proceeding for issuance of a decision on environmental conditions are the applicant and any entity holding property rights to the real estate located in the zone which will be impacted by the venture in the variant proposed by the applicant. The zone in this respect is primarily the terrain in which the venture is to be executed as well the area lying within 100 m of the borders of that terrain.

Offshore wind farms are executed in the exclusive economic zone, which is not part of the territory of the Republic of Poland. No entity can hold ownership of waters and the airspace over waters, or of the floor of the sea under the exclusive economic zone, nor the interior of the earth. Moreover, wind farms are typically executed with a buffer, for example with a width of 500 m from the boundaries of the body of water, for which a permit has been issued for erection of artificial islands, structures and equipment. A consequence of these constraints is that the only entities that will be entitled to be parties to such proceedings are the investors.

In addition to the investor, social organisations can also participate in the proceeding for issuance of a decision on environmental conditions, if the specific organisation was entered in the relevant register at least one year before the organisation requests admission to the proceeding. The same requirement of operating for at least a year before joining the proceeding applies to ecological organisations covered by Art. 44 and following of the Environmental Impact Assessment Act.

A decision on environmental conditions for an offshore wind farm is subject to immediate enforcement. This is a departure from the rule that a decision is not enforceable until the period for filing an appeal expires, and that filing of an appeal stays enforcement of the decision. The law also specifies the period for issuance of a decision on environmental conditions for an offshore wind farm venture of 90 days from filing of the application. A 60-day period is also set for considering an appeal from such a decision, if it is challenged. Significantly, in the proceeding before the higher administrative body and before the administrative court, the decision cannot be set aside or invalidated in its entirety if only a part of the decision, concerning the part of the project involving an offshore wind farm along with the set of equipment for drawing off power, is defective. Failure to issue an environmental decision or consider an

The only entities that will be entitled to be parties to the environmental proceedings are the investors.

appeal within the specified period results in imposition of additional duties on the body considering the matter to notify the parties and the minister for climate of the reasons for the delay, indicating a new deadline for resolving the matter.

Due to its binding character, the environmental decision has an essential impact on the future venture. The statutory elements of the decision are set forth in detail in Art. 82(1) of the Environmental Impact Assessment Act. The environmental decision will include information not only on the technical specifications of the wind farm, but also for example the lighting or colour of the facility. Such decisions commonly include a clause requiring reassessment of the environmental impact in the proceeding for issuance of a building permit.

The environmental decision is also the source of additional duties imposed on the applicant, concerning the project execution phase, the operating phase, and the shutdown phase. These include duties in such areas as:

– The need to limit noise from the piling work and reduce the impact on birds (e.g. by using soft-start procedures)
– Protection of cultural heritage (e.g. notification of archaeological finds)
– The possible discovery of military remnants (e.g. developing procedures related to unexploded ordnance)
– The need to ensure environmental safety if unplanned events arise (e.g. use of vessels whose hulls are not treated with anti-fouling paint containing tributyltin)
– The need to ensure safe navigation (e.g. updating and verifying rescue plans).

Investors are often also charged with duties to oversee the environmental impact of the project by maintaining constant monitoring of benthic organisms (animals living on the sea floor), seabirds, migrating birds, fish, porpoises, and even bats.

The environmental decision will include information not only on the technical specifications of the wind farm, but also for example the lighting or colour of the facility.

Environmental impact assessment

For ventures deemed to always have a significant impact on the environment, which includes offshore wind farms regardless of their capacity, in every case it is essential to conduct an environmental impact assessment.

There are three main stages in an environmental impact assessment:

– Verification of the environmental impact report for the project
– Obtaining the opinions and approvals required by the act
– Ensuring the possibility of public participation in the proceeding.

Under Art. 62 of the Environmental Impact Assessment Act, in the assessment of the environmental impact of a venture, the regional director of environmental protection will define, analyse and evaluate primarily the direct and indirect impacts of the project on the environment, the population, material goods, landmarks, the landscape, the mutual impacts between these elements, and access to mineral deposits. It is also essential to analyse three additional elements:

– The risk of serious breakdowns, natural disasters, and construction disasters
– The possibility and methods for preventing and minimising the negative impact of the project on the environment
– The required scope of monitoring.

One of the key elements of the environmental assessment of the project is verification of the environmental impact assessment report by the authority competent to issue a decision on environmental conditions. The environmental impact assessment report should contain information enabling an analysis of the criteria listed above, and should also contain »

ENVIRONMENTAL IMPACT ASSESSMENT CRITERIA

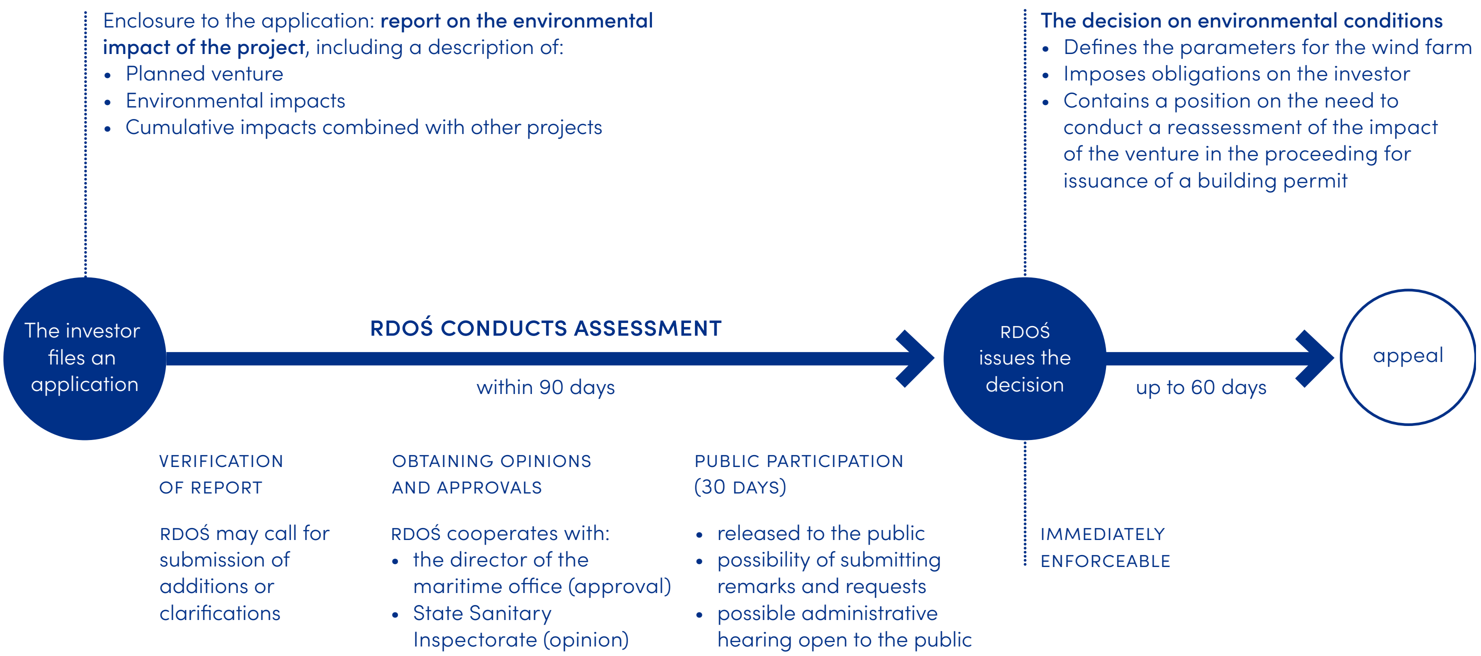
Under Art. 62 of the Environmental Impact Assessment Act, in the assessment of the environmental impact of a venture, the regional director of environmental protection will define, analyse and evaluate primarily the direct and indirect impacts of the project on:

- Environment
- Population
- Material goods
- Landmarks
- Landscape
- The mutual impacts between these elements
- Access to mineral deposits.

Additional elements:

- The risk of serious breakdowns, natural disasters, and construction disasters
- The required scope of monitoring
- The possibility and methods for preventing and minimising the negative impact of the project on the environment.

PROCEDURE FOR ISSUANCE OF ENVIRONMENTAL DECISION
for offshore wind farm



the elements indicated in the Environmental Impact Assessment Act, such as:

– Description of planned venture (Art. 66(1)(1))
– Information on connections with other projects, in particular cumulative impacts of ongoing, completed or planned projects, for which a decision on environmental conditions has been issued, located in the site where the project is planned to be implemented, and in the project's impact area or whose impact is within the area of impact of the planned project, insofar as their impacts could lead to cumulative impacts along with the planned venture (Art. 66(1)(3b))
– Description of the anticipated significant impacts of the planned venture on the environment, including cumulative impacts (Art. 66(1)(8)).

Because the decision on environmental conditions is based on the findings in the environmental impact report, an incomplete report cannot serve as the basis for issuance of a proper environmental decision on the venture (Province Administrative Court in Wrocław judgment of 29 June 2010, case no. II SA/Wr 220/10). Consequently, during

PARTICIPANTS IN THE PROCEEDING

the proceeding the authority may conduct an investigation in which it summons the investor to submit supplements or clarifications of the report as filed. Practice shows that reports that do not specify the location of wind turbines, as well as those that do not present a thorough analysis of the cumulative environmental impact of the project with other offshore wind farm projects, will be considered defective. Such shortcomings may result in refusal to issue a decision on environmental conditions for the project.

Offshore wind energy is the only renewable energy technology available on such a large scale in Poland and also zero-emissions.

In proceedings involving offshore wind farms, the conditions for carrying out the project must be consulted with the director of the relevant maritime office, and an opinion from the relevant body of the State Sanitary Inspectorate must be obtained. It should be pointed out that in the case of projects executed in the Polish exclusive economic zone, no opinion from Polish Waters is required.

Another mandatory stage in the environmental impact assessment is to ensure the opportunity for public participation. Thus the regional director of environmental protection conducting the proceeding must publicise information about filing of the environmental impact report for the project, along with information on the opportunity to examine the report and submit remarks or requests with the authority within 30 days.

Conclusions

Offshore wind energy is the only renewable energy technology available on such a large scale in Poland and also zero-emissions. However, wind farms built in the Polish exclusive economic zone must meet a range of environmental requirements, the most important of which at the initial stage is the environmental impact assessment.

The authority conducting the proceeding on issuance of an environmental decision will take into account the specific nature of the project, its scale and type, and the degree to which it may impact specific aspects of the marine environment.

Potential investors must factor in the possibility of additional and costly obligations. Thus, construction of offshore wind farms should be taken up only by ambitious investors backed by sufficient human and financial resources and experience executing and operating such facilities. This alone can guarantee respect for the rules of protection of the marine environment.

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Developing agricultural and forest land

Businesses that would like to build on farmland or woodland often ask how they can reclassify such land for development and what costs are involved. In this article, we discuss the basic rules and typical fees.

To begin with, a caveat: the colloquial Polish term *odrolnienie* ("de-farming") is used in contexts concerning both the designation of land for purposes other than agriculture and forestry and its removal from production. From a legal point of view, these are two completely different situations. In the article, we will discuss two cases: when there is no agricultural or forestry production on the land (i.e. we are seeking to have the land designated for non-agricultural and non-forestry purposes) and when such production is carried out (i.e. it is a matter of taking farmland or woodland out of production).

For the clarity of the picture, we omit here issues of small scale and area, some specific solutions, reclamation, exceptions and exemptions.

Farmland and woodland: Designation of other land use

Agricultural land and forest land are subject to statutory protection in Poland under the Land Protection Act (Act on Protection of Agricultural Land and Forest Land of 3 February 1995).

The key instrument of protection provided by this act is the restriction of land use for non-agricultural and non-forestry purposes. For non-agricultural and non-forestry purposes, plots designated as barren land in the land registry should primarily be used, or in their absence, other land with the lowest suitability for agricultural production.

The procedural path varies depending on whether the land in question is forest land or agricultural land of classes I–III, or agricultural land in other classes.

Changing the designation of land from the first group requires the approval of the competent authority and an amendment to the local zoning plan. In addition:

- For agricultural land of classes I–III, consent of the minister for rural development is required
- For forest land owned by the state, consent of the minister for the environment is required
- For forest land, consent of the province governor is required, after obtaining the opinion of the agricultural chamber.

If there is no local zoning plan, the use of the listed land for purposes other than agriculture and forestry may be determined by a zoning decision issued in accordance with the Zoning Act (Spatial Planning and Development Act of 27 March 2003). However, under Art. 61(1)(4) of that act, a zoning decision can only be issued if the land was covered by a permit obtained during the preparation of local plans in force in the past, which subsequently expired under the Zoning Act of 7 July 1994 (predecessor to the current act).

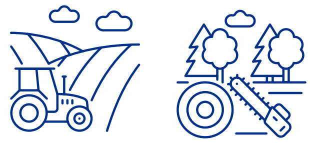
The designation of agricultural land of classes IV–VI for non-agricultural purposes does not have to be done in the local plan, and thus in the absence of a local plan it can be done under a zoning decision, without the restrictions described above arising from Art. 61(1)(4) of the Zoning Act.

Art. 7(1A) of the Land Protection Act provides that the requirement to designate land for non-agricultural and non-forestry purposes in the local plan, requiring the consent of the competent authority, does not apply to land for which a local zoning plan is not prepared. Pursuant to Art. 14(6) of the Zoning Act, a local plan shall not be prepared for closed areas, except for closed areas established by the minister for transport.

"DE-FARMING" UNDER THE LAW

no agricultural or forestry production is conducted on the land

land redesignated for purposes other than agriculture or forestry



agricultural or forestry production is conducted on the land

land removed from agricultural or forestry production

Art. 10A of the Land Protection Act completely exempts agricultural land located within the administrative boundaries of cities from the provisions on restricting the use of such land for non-agricultural purposes contained in Chapter 2 of the act. This is an important provision for those investing in urban areas. Thus, to designate agricultural land located in urban areas for non-agricultural purposes, no administrative permits or corresponding provisions in the local zoning plan are needed. However, if agricultural production is carried out on the land, a decision to take the land out of production must still be obtained (see further below).

The exemption described in the previous paragraph does not apply to woodlands located within the administrative boundaries of cities.

Removal of farmland and woodland from production

Pursuant to the Land Protection Act, removing land from production means the commencement of a land use other than agriculture or forestry. The deed of exclusion requires obtaining a decision from the county executive (*starosta*) with regard to agricultural land or the director of the regional directorate of state forests with regard to forest land.

Pursuant to Art. 11(1) of the Land Protection Act, such decision is required for removal from production of:

- Agricultural land with soils of mineral and organic origin in classes I–III
- Agricultural land with soils of organic origin in classes IV–VI
- All forest land.

Thus, under the act, the protection of forest land is more far-reaching than the protection of agricultural land.

A decision authorising the removal of land from agricultural or forestry production must be enclosed with the application for a building permit or notification of construction or execution of construction works. Thus, a building permit will not be issued if the developer has not obtained a decision to remove the land from production.

Pursuant to the resolution of a seven-judge panel of the Supreme Administrative Court of 3 February 1997 (case no. OPS 13/96), a decision to remove land from agricultural or forestry production shall cover only the area where, under the development plan, the land will begin to be used for purposes other than agriculture or forestry. Excluding the investor's land in its entirety from production contradicts the aims of the Land Protection Act. Thus, the practice sometimes used of excluding land from production "in advance" for further

AUTHORITY ISSUING APPROVAL

DESIGNATION OF ANOTHER LAND USE IN THE PLOT REGISTER

agricultural land classes I–III (outside city limits)	**minister** for rural development
state forest land (outside city limits)	**minister** for environment
other forest lands (outside city limits)	**province marshal** after obtaining the opinion of the agricultural chamber

REMOVAL OF LAND FROM AGRICULTURAL OR FORESTRY PRODUCTION

agricultural land classes I–III mineral and organic soils (also within cities)	county executive
agricultural land classes IV–VI only organic soils (also within cities)	county executive
forest lands	regional director of state forests

development of the property planned for a later stage is not compliant with the act.

In principle, the administrative body cannot arbitrarily refuse to issue a decision to remove land from production. The decision does not lie within the body's administrative discretion. This means that if all the prerequisites provided by law are met, the administrative body is obliged to issue a positive decision, and the application is binding.

Fees for removing land from production

Pursuant to Art. 12(1) of the Land Protection Act, a person who has obtained a permit to remove land from production must pay:
- A one-time fee for permanent removal of the land from production
- An annual fee of 10% of the total amount, payable for 10 years from the time when the land is removed from production.

The amount due shall be reduced by the value of the land determined according to the market prices for land in the given locale on the date the land is actually removed from production (i.e. the value of the land at the time it is removed from production).

The fee for removing one hectare of agricultural land from production is determined depending on the class of land and whether there are soils of mineral or organic origin on the land. The origin of soils can be verified on agricultural soil maps, showing in particular information on the agricultural soil suitability of the area on the basis of depth, texture, structure and content of particles and organic material, stoniness, soil and subsoil erosion, and water-holding capacity, drawn up under the Surveying and Cartography Act of 17 May 1989.

The fee for removing from production one hectare of woodland without standing timber is equal to the price of one cubic metre of timber announced by Statistics Poland, from one of the five forest categories specified in the Land Protection Act.

When forest land is removed from production, a one-time fee is still imposed for premature felling of the standing timber (Regulation of the Minister of the Environment of 20 June 2002).

The removal of agricultural land and forest land from production may take place after the issuance of a decision authorising such removal (Art. 11(1) of the Land Protection Act). A person who has obtained a permit to remove land from production is obliged to pay the dues and annual fees (Art. 12(1)). This obligation arises from the date the land is actually removed from production.

In this context, a purely technical question arises whether all of these issues may be determined in a single decision, or the body should first issue a decision authorising the removal of land from production under Art. 11(1) of the Land Protection Act, and subsequently, after determining the date on which the land was actually removed from production, issue a decision pursuant to Art. 12(1) of the act, setting the amount of dues, annual fees and possible one-time fee

FEES FOR REMOVING LAND FROM AGRICULTURAL OR FOREST PRODUCTION

Farmland fee depending on the class of land and type of soil, less the value of the land on the date of removal from production	One-time fee for permanent removal of land from production	+	Annual fee payable for 10 years		

Woodland fee depending on the category of forest, less the value of the land on the date of removal from production	One-time fee for permanent removal of land from production (1 ha = price of 1 m³ of wood according to Statistics Poland)	+	Annual fee payable for 10 years	+	Compensation for premature felling of trees

for premature logging of the standing timber. The second option was approved in the Supreme Administrative Court judgment of 4 November 2016 (case no. II OSK 224/15) and the Province Administrative Court in Warsaw judgment of 28 February 2017 (case no. IV SA/Wa 2871/16). The act does not explicitly address this issue, but in practice the whole matter is usually determined in a single decision, i.e. the financial obligations (dues, fees, etc) are imposed in the decision removing land from production.

In the case of sale of land removed from production, the duty to pay annual fees is transferred to the purchaser (Art. 12(4) of the Land Protection Act). This provision raises questions of interpretation regarding the situations in which land acquisition occurs. One view is that the land is acquired by virtue of a civil deed transferring the ownership or perpetual usufruct of land. This would mean that taking the land into dependent possession is not acquisition.

Another view was presented in the Province Administrative Court in Lublin judgment of 14 March 2018 (case no. I SA/Lu 986/17), adopting a purposive interpretation according to which the person obliged to pay annual fees is the one who actually benefits from removal of the land from production. This view is supported by the definition of "owner" under the Land Protection Act to mean "also the sole holder, manager or user, perpetual usufructuary, or tenant," and the provision that the person who has obtained the decision to remove land from agricultural or forestry production is required to pay the fees (Art. 12(1) of the Land Protection Act). The basis for justifying the increase in fees is the use of land for non-agricultural and non-forestry purposes. Therefore, the fees are borne by the person using the land. Upon transfer of the right to use the land removed from agricultural and forestry production, the duty to pay the fees passes to the acquirer of this right.

The Land Protection Act requires the transferor to notify the transferee that it will have to pay the fees after acquiring the land removed from production. The act does not link any consequences to the possible lack of such notice, in particular exempting the purchaser from this obligation. However, the vendor's failure to notify the purchaser may constitute grounds for the purchaser's claim for damages against the vendor, as the Supreme Administrative Court held in the judgment of 9 April 2013 (case no. II OSK 2383/11).

The Land Protection Act provides for sanctions for violations of its provisions. Under Art. 28(1), if it is found that land has been removed from production in violation of the act, the perpetrator shall be assessed a fee of twice the amount otherwise due. This applies to land that has not been designated in the local plan for non-agricultural and non-forestry purposes.

Art. 28(2) deals with a situation where the land has admittedly been designated in the local plan for non-agricultural and non-forestry purposes, but has been removed from production without obtaining a decision on removal from production. In such a case, a decision is issued at the authority's own motion to remove the land from production, in which the amount due is increased by 10%.

These fees may not be claimed as operating expenses of persons against whom they are assessed.

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The issues governed by the Act on Protection of Agricultural and Forest Land are relatively complicated, as they combine the fields of planning, zoning, construction, soil typology, forest habitat types, grading of land, and so on. In the absence of local zoning plans, the process of developing land subject to special protection is significantly prolonged.

PAULINA WOJTKOWSKA
Environment practice

Packaging worth its weight in gold

In November 2022 the European Commission adopted a proposal to revise the regulations governing packaging and packaging waste. Among the targets, it was proposed to reduce packaging waste per capita in every EU member state by 2040 by 15% compared to 2018 levels. And soon all packaging should be suitable for recycling. One tool that will undoubtedly help achieve the aims of the proposed regulation is a well-organised deposit system. Such systems currently function in 12 European countries, but are they successful?

What are we collecting?

The report "Management of beverage packaging waste in Poland: Now and in the near future," prepared in 2022 by the Polish Zero Waste Association, found that the overwhelming number of deposit systems in Europe cover three streams of beverage packaging waste: PET packaging (e.g. plastic bottles), metal cans and glass bottles.

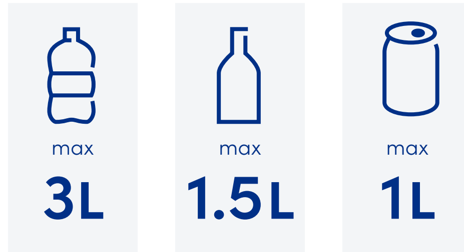
Plastic and metal are collected in all 12 deposit systems currently functioning in Europe (in Croatia, Denmark, Estonia, Finland, Germany, Iceland, Latvia, Lithuania, the Netherlands, Norway, Slovakia and Sweden) and will be collected in all of the six planned systems apart from Poland (in Ireland, Malta, Portugal, Romania and the UK (one system for English & Wales and Northern Ireland and another system in Scotland)). Glass is not covered by the collection system in the Netherlands, Norway, Slovakia or Sweden, nor will it be in Ireland.

Poland initially planned to include in its deposit system only selected **plastic bottles** and **reusable glass bottles** of up to 1.5 litres, but this approach was criticised by stakeholders. Currently, Art. 1(4)(d) of the proposed act implementing a deposit system in Poland provides that the system will cover single-use or reusable beverage packaging included in the draft appendix 1a:

- Single-use plastic bottles of up to 3 l, including bottle tops and caps made of plastic (excluding glass or metal beverage containers with plastic tops or caps)
- Aluminium cans of up to 1 l
- Reusable glass bottles of up to 1.5 l.

> **Alongside PET containers, metal cans are the predominant packaging for beverages in Poland, accounting for 32% of all packaging in this category.**

PLANNED DEPOSIT SYSTEM INCLUDES



A large share of the comments raised in public consultation on the bill to implement a deposit system in Poland concerned **aluminium** and **other metal** beverage containers, which the drafters excluded from the proposed deposit system. The main argument for including **aluminium cans** in the deposit system was that, in the view of NGOs, this is the best way to effectively close the circle for this material, which cannot be ensured by the current practice, which relies only on the price of aluminium. According to the commenters, it cannot be ruled out that in the event of a drop in aluminium prices, there will be less demand for waste aluminium cans, which would consequently have a negative impact on the aluminium recycling rate.

In the second, latest version of the bill, the drafters originally included only **aluminium cans** of up to 1 l, which had to be regarded as a partial success. After all, beverage cans are not produced solely from aluminium, but also from steel, including galvanised steel sheets. These are included in some deposit systems in Europe, but were not covered in the Polish proposal.

This is expected to change soon, as the Deputy Minister of Climate and Environment announced in late November 2022 that these items would be included. Food industry organisations pointed out that alongside PET containers, metal cans are the predominant packaging for beverages in Poland, accounting for 32% of all packaging in this category, and thus this material should not be overlooked.

Contents matter

The type of material from which packaging is made is not the only criterion considered in implementing deposit systems in Europe. The type of beverage also matters, as only water and non-alcoholic beverages (sparkling and still) are basically covered by all currently functioning deposit systems in Europe. The category of "non-alcoholic beverages" may be understood to mean various types of drinks, such as juices, iced tea, diluted juices called "nectars," and energy drinks, and thus it is likely for differences to emerge in this respect across different European countries. Juice and nectar packaging is covered by 8 of the 12 currently functioning deposit systems.

Under Art. 1(4) of the current bill in Poland, "beverage packaging" would be defined as "packaging for liquids intended for immediate drinking, without the need for further processing, *in particular* water, juice, nectar, milk, yogurt or other dairy beverages, or alcoholic beverages, with the exception of liquids that are medicinal products, medical devices or foods for special medical purposes."

The types of beverages mentioned in the bill generally are not controversial within the food industry, except for packaging of milk and dairy products (as we discuss further below).

Stakeholders also raise doubts about overlooking certain types of packaging in the deposit system.

Small liquor bottles outside the system

European countries take different approaches to including packaging for alcoholic beverages within their deposit systems. The report by the Polish Zero Waste Association breaks down in its list the following types of alcoholic beverages: beer, cider, coolers, wine, cordials, and strong spirits. Only Finland has extended its deposit system to all of these categories, making it the only country deciding to charge deposits on packaging of beverages containing over 20% alcohol.

Poland has a chance to expand this group, because, as mentioned, the bill provides that it would cover packaging for liquids intended for immediate drinking, without the need for further processing, in particular alcoholic beverages, regardless of the alcohol content. But this does not mean that collection of alcoholic beverage packaging »

DEPOSIT SYSTEMS IN EUROPE

DEPOSIT SYSTEM

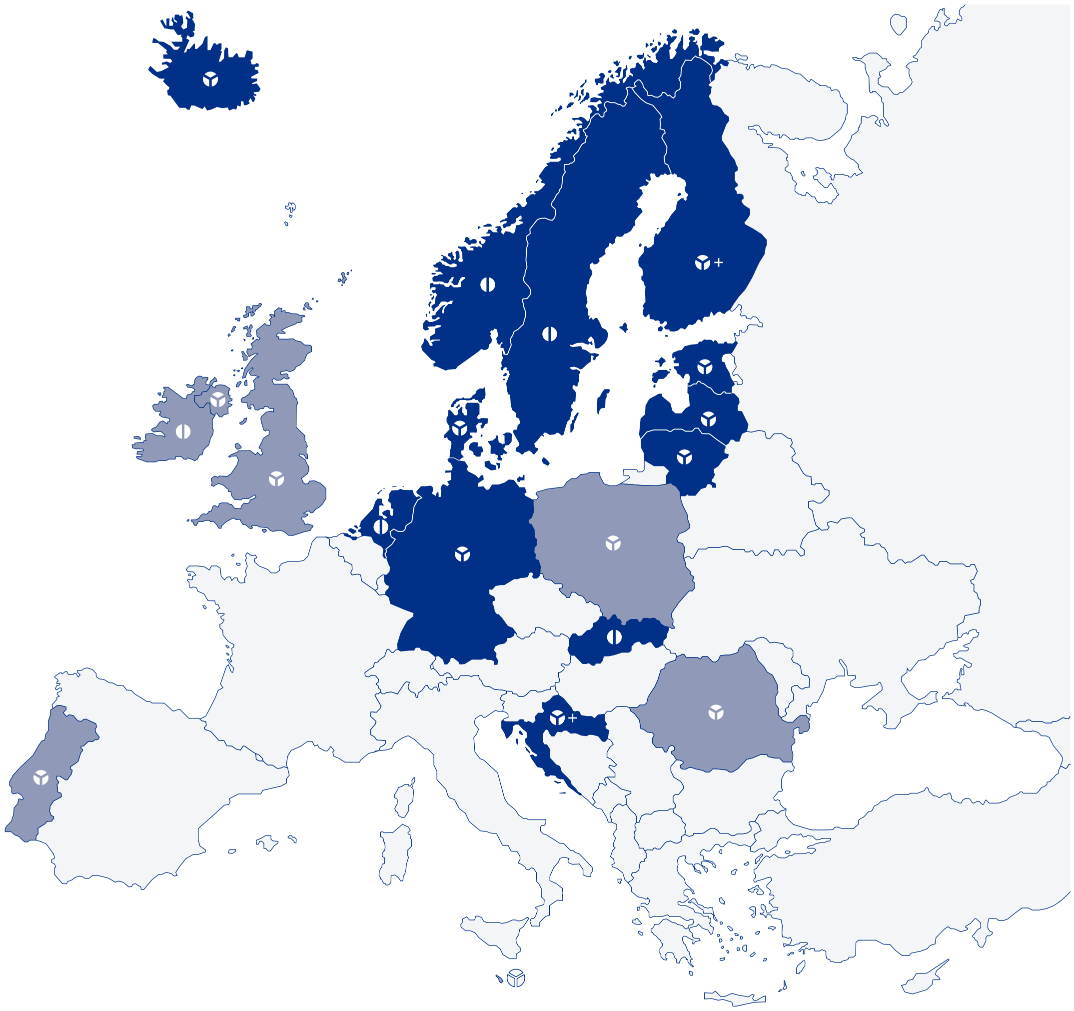
- already in place
- planned

DEPOSIT SYSTEM INCLUDES

- metal/plastic/glass
- metal/plastic

FINLAND
+ all alcoholic beverage packaging

CROATIA
+ milk and dairy product packaging



will be highly effective in Poland. Small spirits bottles of 100–200 ml (colloquially known as *małpki* or "monkeys") would remain outside the Polish deposit system because, contrary to the position previously stated by the Ministry of Climate and Environment, the bill does not cover single-use glass bottles. A study conducted in 2019 by Synergion found that 3 million such bottles are sold every day in Poland, or about a billion a year.

Milk and dairy products under the deposit system

Packaging for milk and dairy products are usually not covered by deposit systems in Europe. An exception is Croatia, which abandoned the practice in 2015 and then restored it in 2021 with the involvement of the NGO Green Action (Zelena Akcija). According to the latest draft, the deposit system in Poland would also cover packaging from beverages such as milk, yogurt and other drinkable dairy products.

However, the food industry in Poland and other European countries does not recommend including milk and dairy product packaging in the deposit system. Their argument relies on sanitary standards. This claim was made in public consultations on the bill by such organisations as the Polish Federation of Food Industry Union of Employers, the Bottling Industry National Chamber of Commerce, and the Polish Breweries Union of Brewing Industry Employers. These organisations all pointed out that storing returned packaging from milk and dairy products on the site of stores would pose a microbial risk to staff and customers, and, particularly at smaller

In 2019 in Poland 3 million single-use glass bottles were sold every day, or about a billion a year.

stores, might discourage consumers from shopping.

It might be argued that extending the deposit system to such packaging would make sense only if consumers returned clean packaging, and such packaging was collected separately from packaging from other types of beverages. But it would be hard to expect all consumers to follow this rule, and such a solution would also give rise to other types of difficulties.

What about multi-material packaging for liquid foods?

It appears, however, that multi-material packaging for liquid foods (e.g. Tetra Pak products) will remain entirely outside the discussion. This issue has been raised primarily by the ProKarton Foundation, whose CEO, Łukasz Sosnowski, asserted at the ENVICON International Environmental Conference in October 2022 that including this type of packaging in the Polish deposit system would enable achievement of a higher level of collection of liquid food cartons, and also increase the reuse rate of this material.

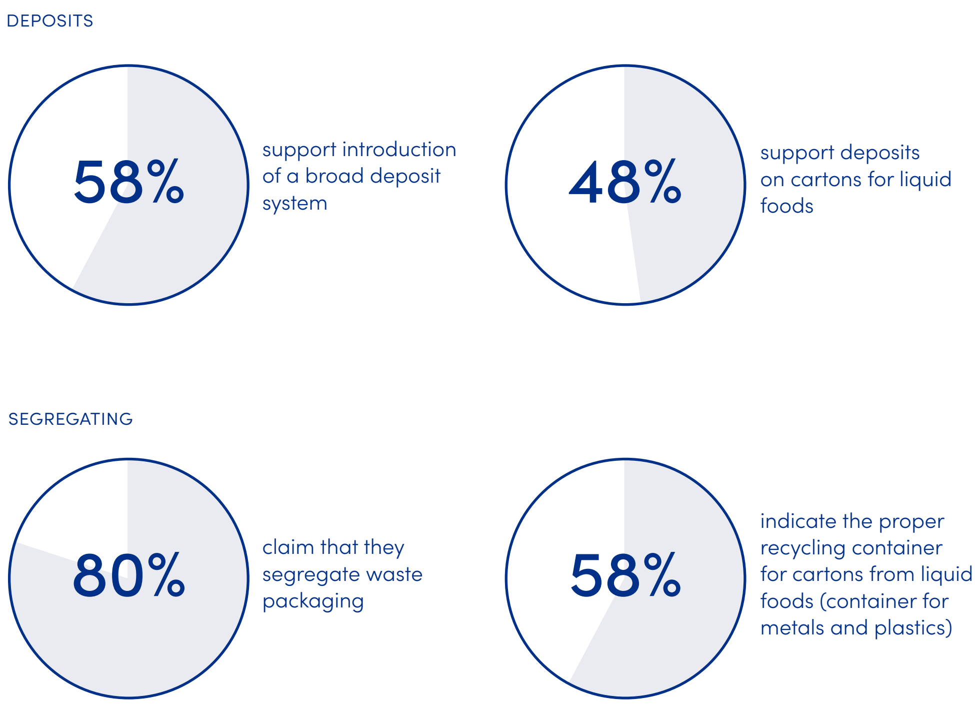
According to a study commissioned by ProKarton and conducted by Kantar Public in September 2022, over half of Poles (58%, up 9 pp from 2019) favour the introduction of a broad deposit system, i.e. also including liquid food cartons, while 48% (3 pp more than in 2019) specifically favour charging a deposit on this type of packaging.

ProKarton's position was not changed by the further findings by Kantar Public that nearly 80% of Poles claim that they segregate packaging waste (although only 58% of respondents correctly indicated the container where they should dispose of such waste, i.e. the container for metals and plastics). But this is undoubtedly an area for further discussion as to the final model of the deposit system in Poland.

Summary

The bill for implementing a deposit system in Poland is broadly similar to the models currently functioning elsewhere in Europe. But this does not automatically mean that the deposit system in the proposed form will be free of defects, which may require new solutions in the future. Some of the problems will probably involve issues discussed above, e.g. packaging from milk and dairy products, 100–200 ml bottles, and multi-material packaging. As work on the bill is ongoing, it may undergo further revisions before adoption.

RECYCLING OF CARTONS FROM LIQUID FOODS IN POLAND



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The equality principle in global supply chains: What will the proposed CSDD Directive change?

2023 is the next phase in enactment of the Corporate Sustainability Due Diligence (CSDD) Directive, drafted by the European Commission. If it enters into force, the directive will require implementation of comprehensive procedures for combatting human rights abuses and harm to the environment in the operations of the biggest corporations and their global supply chains.

The draft directive is an element of the EU policy to meet global challenges such as rapid climate change and the coronavirus pandemic. One of the consequences of these phenomena is deepening social inequality. Thus the new obligations will apply to the biggest companies, whose operations often pose a threat to human rights, including the principle of equality—and not only in the area of employment. Risks also arise in these firms' delivery or receipt of services (particularly in dealings with entities from countries where the principle of equal treatment is not adequately protected), or in other aspects of their own operations (for example "algorithmic discrimination," discussed in more detail below).

It is thus worth considering what sorts of duties will be imposed on companies under the new directive and what they should include in their due diligence policy with respect to compliance with the principle of equality (non-discrimination). What must they require of their longstanding business partners, and how can they enforce it? How should they respond to potential infringements?

Aims of the CSDD proposal

According to a report prepared for the European Commission in connection with work on the draft, some 37% of EU businesses already include due diligence in human rights and the environment in their policies, to varying degrees. The CSDD Directive is designed to set equal rules for all and thus ensure companies and stakeholders legal certainty on the expectations for their operations and the responsibilities imposed on them accordingly.

It will be the duty of the largest market players to identify adverse impacts of their activity on human rights and the environment, and to prevent or minimise those impacts. The proposal also calls for state supervision of their performance of this duty, carrying administrative sanctions, as well as civil liability of corporations to third parties for non-compliance.

The draft directive provides for the need to implement comprehensive procedures for identifying and reducing risks within the operations of the company and its subsidiaries, and within its supply chain, and to remediate adverse impacts if they occur. Among other things, enterprises will have to:

– Integrate due diligence into corporate policy—to have a written due diligence policy, a code of conduct to be followed by employees and subsidiaries, and means of control extending to established business partners
– Identify threats to human rights and the environment in their own operations, and in subsidiaries and supply chains
– Prevent adverse impacts and minimise those that have already occurred, by implementing appropriate preventive procedures, seeking appropriate contractual assurances from business partners, and directing appropriate financial means to implementing such procedures
– Introduce complaint procedures for persons inside and outside the organisation, enabling reporting of any human rights abuses or environmental harm
– Monitor the effectiveness of the adopted due diligence policy
– Communicate information on the company's due diligence policy to the public.

Who will be subject to the proposed obligations?

The first group of addressees includes all companies, regardless of their market sector, who in the last financial year had an average of over 500 employees and net worldwide turnover exceeding EUR 150 million.

The second group is companies with over 250 employees on average and achieving net worldwide turnover exceeding EUR 40 million, deriving at least 50% from selected high-risk sectors of the economy, such as the manufacture of textiles or food products, agriculture, or extraction or trading of mineral resources. The directive will also apply to regulated financial undertakings and companies from outside the EU which generate above a defined threshold of net turnover in the EU.

ADDRESSEES OF THE DIRECTIVE

EMPLOYEES in the last financial year	average of over **500**	average of over **250**
NET WORLDWIDE TURNOVER	over **EUR 150m**	over **EUR 40m**
SOURCE OF NET TURNOVER	any sector	at least **50% generated in high-risk sectors** e.g. manufacturing of textiles or food products, agriculture, extraction or trade of mineral resources

ABOUT

2,600 COMPANIES FROM OUTSIDE THE EU

9,400 COMPANIES IN THE EU

Extending the coverage of the directive only to the biggest corporations has been criticised by non-governmental organisations. A counterargument (raised by, among others, the Polish government, which has approved the wording of the proposal) is the need for gradual, not revolutionary, introduction of the proposed changes. Regardless of the accuracy of this logic, the sector of small and medium-sized enterprises will undoubtedly feel the effects of the proposed regulations indirectly.

Status of the non-discrimination principle in the CSDD Directive

Apart from the climate goals of the directive, one of the main aims is to combat infringements of human rights, and consequently, to respect the principle of equal treatment. This principle prohibits discrimination against anyone due to specific individual characteristics or personal situation, such as sex (including sex characteristics), race, origin, age, physical ability, political affiliation, religion, sexual or gender identity, financial status, or any other circumstances.

The draft CSDD Directive specifies what types of infringements of human rights are covered by the due diligence obligation, cross-referencing a list set forth in Annex I to the directive. Not every infringement will be covered by the proposed obligations.

The principle of equal treatment plays a key role here. It will be a mandatory feature of a company's due diligence policy only in the area of employment, in particular equal pay for work of equal value. But this aspect of non-discrimination is already the law in all EU member states, under both national and EU regulations.

The general principle of equal treatment reaches further. It may apply not only to employment, but also to goods and services —how they are offered and used by the company. This aspect of equal treatment may be tackled via policies for purchasing and delivery of services, using appropriate anti-discrimination clauses.

Apart from the climate goals of the directive, one of the main aims is to combat infringements of human rights, and consequently, to respect the principle of equal treatment.

Other example of adverse impacts for social equality in the operations of companies would be the activity of international IT firms using algorithms based on artificial intelligence. Noteworthy in this respect is the recent report by the European Commission entitled "Algorithmic discrimination in Europe," on threats to equal treatment flowing from the operation of online algorithms. The report provides an extensive discussion of situations in which discrimination may occur through the operation of AI-based algorithms—perpetuating stereotypes (racial, gender, social or other) in search results, targeting of online ads, profiling of services, or software used by HR departments.

Combating discrimination in supply chains

In the context of such atypical threats to equality, the last point of Annex I to the proposed CSDD Directive is particularly noteworthy. This provision expands the catalogue of human rights infringements covered by the directive to include rights not expressly listed in the directive. It is sufficient if the rights are set forth in any of the international human rights instruments referred to in the annex, and that the company could reasonably foresee such human rights abuses taking into account the circumstances of its operations, the operational sector and the operational context.

The principle of equality appears in most international agreements concerning human rights, such as the United Nations International Covenant on Civil and Political Rights, cited in Annex I to the directive. Thus if it turns out that the activity of a company or entities in its supply chain may be tied to infringement of the broad principle of equal treatment, this risk should be mitigated in all the areas of the obligations set forth in the CSDD Directive.

The principle of equality may also be reflected in contractual assurances which the company may demand from its business

EXAMPLE **THE PRINCIPLE OF EQUALITY**

A credit institution uses an AI-based algorithm to determine the creditworthiness of potential borrowers. Under the CSDD Directive, the institution would have to conduct an audit of its operations for the risk of discrimination. If it turned out that the operation of the algorithm privileged, for example, the group of men over age 35, perpetuating gender stereotypes on economic grounds, the institution would have to implement appropriate measures and modify the algorithm so it no longer privileged any social group.

The principle of equality may also be reflected in contractual assurances which the company may demand from its business partners.

partners. This could apply in particular to entities from countries with a high risk of infringement of human rights, e.g. countries that do not respect the principle of gender equality or do not sufficiently protect the rights of LGBTIQ persons.

Summary

The CSDD Directive offers an opportunity to improve implementation of the principle of social equality. Although the principle of non-discrimination as a fundamental human right is expressly stipulated in the proposal only in the area of employment, this would not relieve the biggest companies from the duty to examine risks of infringing this principle across all areas of their operations.

Such risks might arise in a company's employment policy (e.g. as a result of gender discrimination for managerial positions), in the operation of subsidiaries or in specific links in the value chain (e.g. in a third country where minority rights are poorly protected), and in the consequences of its operations (e.g. perpetuation of stereotypes via AI-based algorithms).

If such risks are identified, the company will be required to take appropriate remedial measures, set forth in a written due diligence policy, and also, depending on the case, to obtain appropriate contractual assurances from partners within its established business relationships.

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ESG & Sustainability practice

ESG: Allies of business and the environment

Sustainability a long time ago ceased to be a mere add-on to business strategy. It is now a lodestar followed by regulators and financial institutions. Companies failing to understand this may have problems remaining competitive or obtaining financing.

Indeed, redirecting capital flows into sustainable investment for the purpose of achieving sustainable and inclusive growth is one of the overarching long-term goals of the European Commission. A Bloomberg study found that sustainable investing has gone mainstream, with an estimated USD 37.8 trillion in assets under management in 2022. According to the same study, global ESG assets may exceed USD 53 trillion by 2025.

What is ESG used for and what does it cover?

ESG (environmental, social, governance) criteria are used for non-financial evaluation of economic activity and address three aspects:
- Environmental protection and prevention of environmental degradation
- Social responsibility and human rights
- Corporate governance.

The environment area covers, for example, the use of energy sources, consumption of utilities, generation of wastes and methods of waste disposal, emission of pollutants and supply of raw materials.

In social responsibility, the issues under scrutiny include respect for human rights in the supply chain, equal pay, respect for employees rights, data security, and promotion of equality.

Ultimately sustainability information will have a status comparable to financial information.

The third aspect, corporate governance, is particularly important for long-term investors, as it affects confidence in the company and its business operations. In this regard, ESG analyses issues of executive compensation, the structure of corporate authorities, and oversight. It also seeks to ensure compliance with duties to keep shareholders informed and implementation of fiscal transparency and anti-corruption measures.

When business is sustainable

In this regard, guidance is provided by the EU's Taxonomy Regulation (2020/852), which establishes a classification system for environmentally sustainable economic activity. According to the regulation, an activity can be deemed sustainable if it contributes substantially to one or more of the following environmental objectives:

- Climate change mitigation
- Climate change adaptation
- Sustainable use and protection of water and marine resources
- Transition to a circular economy
- Pollution prevention and control
- Protection and restoration of biodiversity and ecosystems.

At the same time, the activity must not significantly harm any other environmental objectives. The activity should also be conducted in compliance with minimum safeguards (e.g. the OECD Guidelines for Multinational Enterprises) and meet technical screening criteria established in separate legal acts.

For example, an economic activity can make a significant contribution to achieving the goal of transitioning to a circular economy by increasing product durability, repairability and improvement, and reuse or reduction of resource consumption through appropriate design and material selection with the goal of making products, components and materials as useful as possible for as long as possible.

Establishment of criteria for classifying economic activity as environmentally sustainable is also intended to encourage businesses not subject to non-financial reporting to voluntarily publish and disclose data on their environmentally sustainable activities. This information will not only help financial market participants and other entities in the financial markets to easily determine which businesses are operating sustainably, but will also make it easier for sustainable businesses to raise funds to conduct and develop these activities.

Non-financial ≠ financially insignificant

One might get the impression that the term "non-financial indicator" implies that information pertaining to sustainability is not financially meaningful, but only adds a gloss of corporate social responsibility. Nothing could be further from the truth. ESG affects a company's long-term shareholder value and demonstrates its impact on society and the environment. Measures taken at the EU and national levels are ultimately intended to lead to a situation where sustainability information has a status comparable to financial information. There is already a terminological shift from "non-financial reporting" to "sustainability reporting."

Who will be required to report on sustainability?

Until now, non-financial reporting has applied to large listed companies, credit institutions and insurance companies employing more than 500 people at certain thresholds: EUR 20 million in total assets on the balance sheet at the end of the fiscal year, or EUR 40 million in net turnover from sales of products and services for the fiscal year.

On 14 December 2022, the Corporate Sustainability Reporting Directive (CSRD) was adopted at the EU level. This will expand the number of organisations required to publish non-financial information from 1 January 2025 (disclosures in 2026), to cover all large companies (public and non-public) meeting at least two of the following criteria: average employment of at least 250 people, balance sheet total of at least EUR 20 million, or net turnover of at least EUR 40 million.

Also, as of 1 January 2026 (disclosures in 2027), public small and medium-sized enterprises, small and non-complex credit institutions and captive insurance undertakings will be required to prepare non-financial reports. After that date, during a two-year transition period (until 2028), SMEs will be able to skip non-financial

»

WHO IS REQUIRED TO REPORT ON SUSTAINABILITY

currently
reports according to new CSRD rules in 2025 for fiscal year 2024

- LARGE LISTED COMPANIES
- CREDIT INSTITUTIONS
- INSURANCE COMPANIES

average of over **500** employees and balance sheet total of more than **EUR 20m** or net turnover of more than **EUR 40m**

as of 1 January 2025
disclosures in 2026

- REMAINING LARGE COMPANIES
- CAPITAL GROUPS (public and non-public)

If at least **2 of 3** conditions are met:

average of over	balance sheet total of more than	net turnover of more than
250 employees	**EUR 20m**	**EUR 40m**

as of 1 January 2026
disclosures in 2027

- SMALL AND NON-COMPLEX CREDIT INSTITUTIONS
- CAPTIVE INSURANCE UNDERTAKINGS
- PUBLIC SMEs (according to separate, simplified standards to be developed by EFRAG in 2023)

reporting, provided that they briefly indicate in their management report why sustainability information has not been reported.

The disclosure of non-financial information will remain voluntary for unlisted SMEs. However, in practice, it may also turn out that entities not required to prepare reports in this regard will report on the environmental impact of their activities. Among other things, this will be driven by the expectations of counterparties obliged to disclose information on value and supply chains, as well as consumers who consider issues of environmental impact of products and services in their purchasing decisions.

What information should be reported

The information reported under ESG indicators should relate to the future and the past and include both qualitative and quantitative data, and when possible should be based on scientific evidence. The information should also be harmonised, comparable and, where appropriate, based on uniform indicators, while allowing reporting that is specific to individual units at the same time. Also, the reported sustainability information should take a short-, medium- and long-term perspective and include information on the company's entire value chain, including its own operations, products and services, business relationships and supply chains.

If not all the necessary information on the company's value chain is available, the company should indicate:

– What efforts it has undertaken to obtain the missing information
– Why the information could not be obtained
– What actions it plans to undertake to obtain all the necessary information in the future.

The information reported under ESG indicators should relate to the future and the past and include both qualitative and quantitative data.

Why is it worthwhile?

In short, to become more transparent, attractive to contractors and consumers, and environmentally friendly.

Also, the advantages of introducing ESG factors into a company's operations are widely discussed by the European Commission. On 17 June 2019, in a communication entitled "Guidelines on non-financial reporting: Supplement on reporting climate-related information," the Commission highlighted the benefits for companies reporting climate-related information, in particular, increasing company awareness and understanding of climate-related risks and opportunities, diversifying the investor base, lowering the cost of capital, and more constructive dialogue with all stakeholders. Additionally, diversity on corporate boards can contribute to better decision-making, corporate governance and resilience to crises.

In turn, companies can benefit by conducting high-quality reporting on sustainability issues. The increase in the number of investment products to achieve sustainability goals means that good sustainability reporting can increase the company's access to financial capital.

Companies should bear in mind that the introduction of real and meaningful changes, beneficial from the point of view of non-financial indicators, will not be possible if employees and business partners do not realise the need to change existing practices, and the reasons for doing so. In practice this means educating employees, board members, counterparties and distributors throughout the supply chain.

Importantly, ESG should not be treated as an indicator available and achievable only to a selected group of businesses, as ESG also ultimately translates into business that is profitable, long-term, sustainable, responsible, and beneficial to society. Therefore, it is worthwhile to get into the swim of the current changes, to avoid being left behind, while at the same time contributing to improvement of the environment.

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ESG and M&A: How sustainability is shaping the mergers and acquisitions market

Duties concerning environmental, social and governance issues provided for in current and planned legal regulations, along with growing expectations of investors and consumers, mean that sustainability is playing a greater and greater role. It is worth examining how the ESG trend is impacting mergers and acquisitions.

What is ESG?

Some time ago, the once popular notion of corporate social responsibility evolved into the more expansive concept of ESG, which postulates that the value of a company is measured not just by profit, but also includes non-financial aspects affecting the environment, society, and corporate governance.

Prized and valued

Many studies show the link between a company's treatment of ESG concepts and the company's investment appeal. Devoting attention to sustainability factors contributes not only to building the company's reputation, but also to increasing the market value of its shares, improving operating and financial efficiency, and even higher output by employees. Companies lacking an ESG strategy or lagging in implementing it are already perceived as carrying a higher level of transactional risk, and will be even more so in the future. This has a direct impact on the company's valuation, as investors deciding on committing their capital have already begun to take into account whether the company factors environmental, social and governance into its business. The absence of an appropriate ESG strategy can thus reduce a company's competitiveness, which may in turn (as the significance of ESG rises) also limit its access to financing, or in extreme cases could even sideline the company from the M&A market altogether.

THE LETTERS IN THE ACRONYM COVER A RANGE OF ISSUES, SUCH AS

E Enviromental

- Greenhouse gases
- Energy consumption
- Management of water resources
- Generation and recycling of packaging
- Hazardous waste
- Soil contamination and erosion
- Rights of animals and protection of endangered species
- Ecology

S Social

- Human rights
- Occupational health and safety standards
- Product safety
- Diversity management
- Employer–employee relations
- Relations with the local community

G Governance

- Cybersecurity
- Anticorruption policy
- Whistleblowing procedure
- Ethical standards
- Gender parity in corporate authorities

Due diligence and ESG

Certain issues related to ESG have been commonly included in due diligence for quite some time. These include selected topics related to the environment, worker health and safety, anticorruption policy, and cybersecurity. Other aspects of ESG are only beginning to assume importance and appear as separate categories for legal analysis in due diligence. Increasingly, separate due diligence reports devoted to ESG can be encountered comprehensively examining sustainability factors with reference to the target. The driving force behind this approach is most often the desire of potential investors who realise the reputational risk and financial risk arising from failure to comply with ESG standards, and demand greater transparency from companies in this respect.

ESG due diligence reports focus primarily on examining whether the company meets ESG standards and complies with national, international and EU sustainability regulations.

It is important to add that the significance of ESG factors with respect to the M&A market is manifest not only in the due diligence phase, but also, as a consequence of that phase, when negotiating and drafting the transaction documents and in post-closing activities. Sustainability issues increasingly appear in the representations and warranties and in strategies following the closing of the transaction.

In terms of ESG laws, EU regulations and directives implemented into national law of particular note include:

– Non-Financial Reporting Directive (2014/95/EU) (NFRD)
– Sustainable Finance Disclosure Regulation (2019/2088) (SFDR)
– Taxonomy Regulation (2020/852)
– Corporate Sustainability Reporting Directive (2022/2464) (CSRD), which entered into force on 5 January 2023; the member states have until 6 July 2024 to introduce regulations needed to comply with the directive
– Proposed Corporate Sustainability Due Diligence (CSDD) Directive (still working its way through the legislative process).

Two directives, CSRD and CSDD, expand the scope of due diligence on ESG issues. The CSRD modifies the current reporting rules set forth in the NFRD by broadening the group of entities required to report and introducing common reporting standards. In turn, the CSDD Directive will establish duties with respect to actual or potential negative impacts for the environment and human rights arising out of a company's own operations, the operations of its subsidiaries, and throughout the value chain via entities with which the company maintains ongoing business relations, and will also address the issue of liability for breach of these obligations. »

PE, VC and big companies have already put ESG in play

The opportunities arising out of ESG were spotted some time ago by private-equity and venture-capital funds, for whom issues associated with sustainability sparked the creation of value and growth. PE and VC funds leverage ESG issues to acquire companies, responsibly manage their portfolios, and achieve better results when exiting the investment.

In the case of some companies, implementation of ESG principles is a consequence of the openness to this topic on the part of management. But there are companies that have been required to take account of ESG factors because of legal regulations imposed on them. Under the provisions of the Accounting Act implementing the NFRD into Polish law, since 2018 companies meeting certain criteria (e.g. large listed companies, banks and insurers) have had to file statements or reports on non-financial information. In the upcoming years the CSRD will expand the set of companies that must report on sustainability. Consequently, more companies will have to reflect ESG principles in their day-to-day operations and, when growing, in their acquisition policy.

Summary

ESG aspects are exerting an impact on the mergers and acquisitions market. They are relevant when assessing transactional risk, they affect the valuations of companies, and they can even be a condition for raising financing for transactions. Sustainability is already gaining a higher profile during due diligence, is increasingly included in representations and warranties, and is more and more often integrated into post-closing strategies.

The private-equity and venture-capital industries are actively pursuing ESG principles, recognising in sustainability a new opportunity for value creation and growth—not to mention companies already covered by the NFRD, implemented in the Accounting Act, for whom ESG has been a focus for several years, or companies that will fall into the expanding circle of entities required to maintain sustainability reporting under the CSRD.

For these reasons, the influence of sustainability on the M&A market is a fascinating and important topic worth examining not only in 2023, but for years to come.

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Squeeze-out and sell-out in a limited-liability company

The new Holding Law entered into force in Poland on 13 October 2022. It introduced into the Commercial Companies Code provisions governing the operation of corporate groups, including the possibility of a forced exit for shareholders in a limited-liability company.

Article includes sections of an article previously published on the In Principle portal.

What are the changes?

The amendments known as the "Holding Law" introduced solutions aimed at streamlining the management of corporate groups by the parent company and pursuit of the common aims and strategies of the group. At the same time, provisions were adopted aimed at protecting minority shareholders within a corporate group, subsidiaries, creditors, and members of the authorities of subsidiaries and parent companies.

Thus, for example, it was recognised that **within an established corporate group, a company participating in the group should be guided by the company's own interests but also by the interests of the group**. But this must not come at the expense of injury to the subsidiary's creditors or minority shareholders. The possibility for the parent company to issue **binding instructions** to the subsidiary was provided for, as well as **conditions where the subsidiary must refuse to carry out such instructions**. This is designed to protect the minority shareholders and creditors. An **exclusion of liability** to the company on the part of the company's management board was adopted in cases where the management board carries out binding instructions. The amendment establishes grounds for the parent company's liability:

- To the subsidiary for injury caused to the subsidiary
- To minority shareholders of the subsidiary for the reduction in value of their shares as a result of issuance of binding instructions
- To creditors of the subsidiary.

Among the new provisions, two solutions are particularly noteworthy, involving protection of minority shareholders of a limited-liability company through **squeeze-out** of their shares and their **right to sell out** their

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shares. As a rule, no such possibilities existed in a limited-liability company (sp. z o.o.), although squeeze-out and sell-out were possible in a joint-stock company (SA). The new rules for limited-liability companies were modelled on those for joint-stock companies, which they partially cross-reference. Thus it will be possible to interpret the newly introduced regulations governing limited-liability companies in light of the case law and legal literature developed in relation to joint-stock companies.

Squeeze-out and sell-out before adoption of the Holding Law

Prior to 13 October 2022, rules governing squeeze-out and sell-out of the minority to the majority were generally provided only with respect to a joint-stock company, and those rules remain in force.

A resolution in a joint-stock company to squeeze out minority shareholders requires a majority of 95% of the votes in open, named voting, by no more than five shareholders, each holding at least 5% of the share capital, unless the articles of association impose stricter requirements for a squeeze-out. In such voting, each share carries one vote (without privilege or restriction).

The price for purchase of the shares in a squeeze-out is determined by an appraiser appointed by the general meeting or the registry court at the company's request. Announcement of the resolution commences the running of the period for the shareholders being squeezed out to submit their shares. The persons buying out the shares are required to pay the purchase price for the shares to the company's account. Payment of the purchase price by the majority shareholders is a necessary condition for the effectiveness of the entire squeeze-out procedure.

Minority shareholders of a joint-stock company can now also force a buyout of their shares. One or more shareholders representing no more than 5% of the share capital may demand inclusion in the agenda for the next general meeting of a resolution on buyout of their shares by no more than five shareholders together representing no less than 95% of the share capital, each of whom holds at least 5% of the share capital (majority shareholders).

If the sell-out resolution is not adopted, the company is then required to purchase the shares of the minority shareholders, and the majority shareholders are liable to the company for payment of the entire sell-out price.

In a sell-out of shares, the share price is equal to the net asset value per share indicated in the financial report for the last financial year, less the amount earmarked for distribution to the shareholders. Minority shareholders can also demand that the court appoint an appraiser to establish the market value or fair value of the sell-out shares.

Other methods for removing shareholders

Under current law, it is possible to seek to **exclude a shareholder from a company**. But this is not a quick and simple method for parting ways, as it is necessary to file suit and obtain a judgment from the court.

For example, in a limited-liability company, the court may order the exclusion of a shareholder from the company for serious cause concerning the shareholder in question, at the request of all of the other shareholders, if they hold more than half of the share capital (Commercial Companies Code Art. 266). The price for taking over the shares is set by the court. But it is necessary to show "serious cause," and thus, for example, significant disruption or the impossibility to conduct the business of the company. Based on the case law, such actions might include conducting competing activity, acting to the detriment of the company, or abuse of the right to inspect the affairs of the company.

Another method for removing shareholders from a company is **redemption of their shares**, which, assuming the shareholder whose shares are to be redeemed does not consent, would have to be an involuntary redemption. But this type of redemption is permissible only when the articles of association allow it and specify the grounds for involuntary redemption (Commercial Companies Code Art. 199). Thus at the stage of drafting the articles of association it would be necessary to predict in advance, and describe as precisely as possible, the grounds, procedure and rules for the redemption. In the case of conflict between shareholders, exercise of this procedure often ends up in litigation initiated by the shareholders whose shares are to be involuntarily redeemed.

In practice, to ensure the possibility for a shareholder's exit from the company, solutions are agreed within the bounds of the principle of freedom of contract, such as put options, call options, drag-along rights and tag-along rights.

Put options may entitle minority shareholders to sell their shares to the majority shareholder, while **call options** may entitle the majority shareholder to acquire shares of a minority shareholder. These options thus bear a certain similarity to the statutory rights of sell-out and squeeze-out.

A **tag-along right** entitles a shareholder to join a sale when another shareholder (typically the majority shareholder) sells its shares to a third party. A **drag-along right** entitles a shareholder (typically the majority shareholder) to force a minority shareholder to sell its shares when the first shareholder sells its shares to a third party.

As in the case of redemption, these solutions require detailed contractual regulation at the stage when the shareholders are cooperating within the company, particularly defining the grounds for exercising these rights, the timing, and the price for the shares or the method for calculating the price.

New method of squeeze-out and sell-out only within a corporate group

The Holding Law provisions in force since 13 October 2022 introduce additional possibilities for demanding the sale or purchase of shares and also apply to limited-liability companies. However, they can be exercised only in a company "participating in a group of companies."

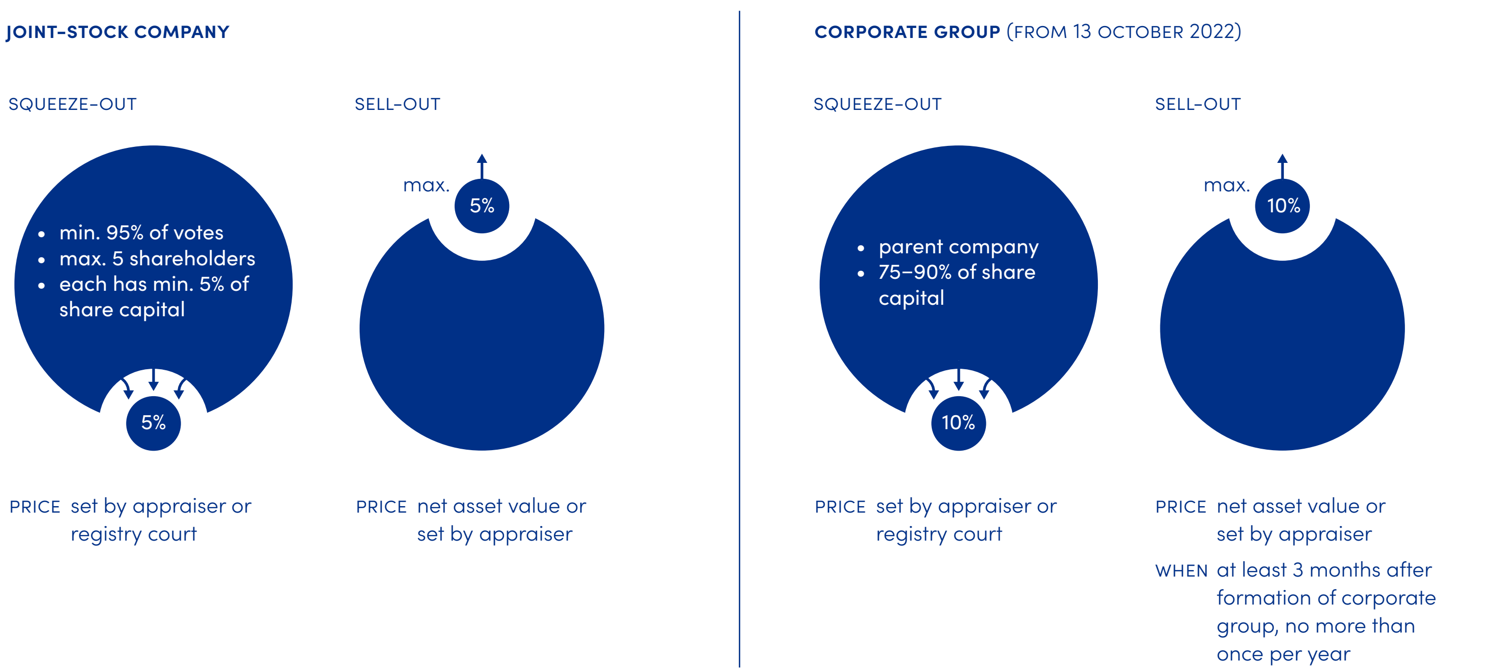
The new regulations permit the shareholders of a subsidiary to adopt a resolution (by a three-fourths majority of votes) on the subsidiary's joining a corporate group. This type of control will be disclosed in the commercial register, and the parent company may issue binding instructions to the subsidiary concerning the subsidiary's affairs. Thus, the regulations on squeeze-out and sell-out of shares in a limited-liability company cannot be applied with respect to every such company or in any kind of capital group, but only within a formally established corporate group, with respect to a company participating in such group.

Squeeze-out is a tool enabling the majority shareholder to deal with disruptive minority shareholders by buying out their shares. Sell-out, conversely, protects minority shareholders and creates a possibility for exiting the company, particularly in a situation where the majority shareholder is abusing its dominant position. These rights are similar in the sense that in each case, the minority shareholder ceases to be a shareholder, and the price for the shares is set by an appraiser.

Squeeze-out of shares in a limited-liability company participating in a corporate group

The new Holding Law introduced the possibility of squeezing out shareholders in both a limited-liability company and a joint-stock company (Commercial Companies Code Art. 21^{11}). The shareholders' meeting of the company may adopt a resolution on mandatory buyout of the shares of shareholders representing no more than **10%** of the share capital by the parent company, directly representing at least **90%** of the share capital. The articles of association may set a threshold lower than 90%, but no lower than **75%** of the share capital.

Otherwise, the procedure for squeeze-out of a shareholder in a limited-liability company participating in a group of companies will also be governed by certain provisions concerning squeeze-out of a shareholder in a joint-stock company (not participating in a group of companies), including the provisions on the method of determining the price. »



Another method for squeezing out a minority shareholder by the majority shareholder is to introduce certain changes in the articles of association over the objection of the minority shareholder. A subsidiary (other than a wholly owned subsidiary) participating in a group of companies is required to refuse to execute a binding instruction if there is a justified concern that it conflicts with the interests of the subsidiary and will cause an injury to the subsidiary which will not be redressed by the parent company or another company in the group.

The articles of association of a subsidiary participating in a group of companies may provide for additional grounds for refusal to execute binding instructions. The effectiveness of a resolution amending the articles of association which

– Introduces such additional grounds, or
– Reduces the threshold of 90% of the share capital (to 75% at the lowest) enabling squeeze-out of minority shareholders

depends on the company's buyout of the shares of the shareholders who do not agree to the change and assert a demand to have their shares bought out. The price for the shares will be determined by an appraiser appointed by the shareholders' meeting, or if the shareholders' meeting does not select an appraiser, the appraiser will be appointed by the court (at the request of the management board).

The new regulations under the Holding Law are also intended to facilitate the exit from a company by minority shareholders who do not wish to participate in a company that is formally part of a corporate group.

Sell-out of shares in a limited-liability company participating in a corporate group

A minority shareholder representing no more than 10% of the share capital of a subsidiary participating in a corporate group may demand inclusion in the agenda of the next shareholders' meeting (or general meeting) of a resolution on compulsory buyout of its shares by the parent company representing (directly, indirectly or in concert with other persons) at least 90% of the share capital of the subsidiary participating in the group of companies.

The regulations include two temporal restrictions on the right of sell-out. First, a sell-out demand may not be submitted sooner than three months after disclosure in the register of the subsidiary's participation in the corporate group. Second, a sell-out demand may be submitted only once within a financial year.

Because this provision refers to the "parent company," it might seem that this entitlement is not vested in a shareholder who is a natural person. This distinction appears unfounded. It limits the right of a minority shareholder to demand to sell out when the dominant shareholder is a natural person.

As in the case of squeeze-out, the new provisions call by cross-reference for application as relevant of the provisions on the sell-out of shares in a joint-stock company, including with respect to the method of demanding the sell-out, the mechanism for setting the price, and the method of payment. It should be stressed in this regard that minority shareholders remain shareholders and retain their rights until the price for the sold-out shares is paid.

Summary

Only the practice will show whether the new regulations on issuance of binding instructions and liability of corporate authorities (see "Binding instructions within corporate groups," p. 65 below) prove beneficial enough for existing, informal corporate groups that they decide to adopt resolutions establishing formal corporate groups. Also before the change, corporate groups operated in a manner enabling them to appropriately manage the affairs of a set of companies in compliance with the policy of the group.

Certainly the new provisions introduce solutions favourable to majority shareholders of companies participating in corporate groups who wish to part ways with minority shareholders. The threshold enabling use of these solutions is lower than the threshold for a joint-stock company not participating in a corporate group (generally 90% under the Holding Law, and in certain instances as little of 75% of the share capital, instead of 95%). Moreover, a squeeze-out may be conducted based on the new provisions also in a limited-liability company (participating in a corporate group). Formal corporate groups may therefore allow majority shareholders to squeeze out minority shareholders from limited-liability companies.

On the other hand, under the new regulations, minority shareholders not wishing to remain in a company that is part of a corporate group can at their own initiative force the buyout of their shares. This right of sell-out is essential for protection of minority shareholders, particularly in corporate groups. Without it, in practice, within a limited-liability company it can be extremely difficult, if not impossible, for a minority shareholder to exit the company. If one shareholder dominates the company, the other shareholders have no influence over the operations of the company, and often in such cases a dividend is not distributed. Such minority stakes are typically hard to sell, which often means that it is hard to obtain a fair market price for them, as the majority shareholder may prove to be the only potential buyer. Therefore it would appear to be a just solution to introduce such rights for minority shareholders in all limited-liability companies, not only those participating in a formally established corporate group.

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Alternative methods for settling the purchase price in M&A transactions

It might seem that in share deals, someone sells shares and someone else buys them, paying the agreed price in exchange. And that's all. This is obviously a model situation and greatly simplified. But it doesn't necessarily happen in practice.

M&A practice forces the parties to consider applying alternative payment methods. Some of these methods might seem complicated, but only on the surface. In fact, applying some other solution in the given instance than a straightforward cash payment often serves to simplify the settlement of the price between the parties.

The types of transactions we are discussing here are share deals, which essentially involve acquisition of the company itself, as the aim of the acquisition in the great majority of cases is for the buyer to acquire at least a majority stake in the shares and then use this stake to exercise real control over the target company. The company is on one hand a separate entity from its shareholders (formally and practically), but it is also an entity that cannot function in isolation from its owners. Particularly in the case of large corporate groups, the specific company usually pursues the aims entrusted to it by the group. It is the subject of various contractual relations: bank credit, loans from shareholders or third parties, and so on. Paying down all these obligations before the transaction is not usually possible —if for no other reason, because neither the company nor its owners (the sellers) have sufficient funds on hand (it is only the transaction that will allow the sellers to convert their shares into cash).

Buyer's payment of the company's obligations

Shareholder loans are a frequently encountered method of financing the operations of a company. As long as the shareholders remain in the company, this tool is quite flexible. It allows the company access to funds on (generally) more favourable terms than bank credit. It also allows the shareholders to profit in the form of interest on their loans. Finally, as needed

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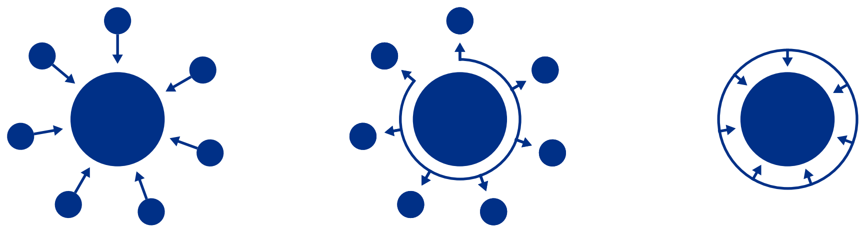
it allows such obligations to be converted into share capital of the company (as a result of which the shareholder ceases to be a creditor and the company a debtor, and in exchange the shareholder receives more shares in the company).

In the case of a decision to sell a company, the company usually does not have adequate funds on hand to pay down its obligations to shareholders in full. Therefore, often an element of the transaction is for the company's obligations to the shareholders (the sellers) to be paid off by the buyer. In that case, the buyer, by paying the company's obligations, enters (with the company's consent) into the rights of the satisfied creditor (the former shareholder), thus becoming a creditor of the company (and also a shareholder of the company, due to simultaneous acquisition of its shares). This results in "subrogation" (Art. 518 §1(3) of the Polish Civil Code). From a purely financial point of view (leaving aside here the issue of the need for the buyer to have the necessary amount of cash on hand to pay off the company's obligations) this is a neutral operation for the buyer. Although the buyer is forced to pay more than the "clean" price for the company, in exchange it "acquires" a claim against the company which is now the buyer's own.

Non-cash consideration in place of payment of the purchase price

A somewhat different situation occurs when the parties agree that in settlement of the transaction, the price (or usually a portion of the price) will be paid by the buyer in some method other than cash. This happens in particular in instances where the buyer is a larger entity, and the parties agree that upon sale of the shares in the company, the seller will also become a shareholder (generally holding a minor stake) of the buyer (or of a subsidiary).

REPAYMENT OF SHAREHOLDER LOANS

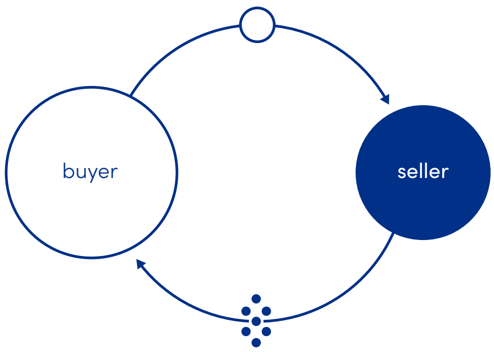


Shareholders finance company, company owes them debt

Acquirer pays off shareholder loans

Acquirer assumes the shareholders' rights, company owes it debt

TRANSFER OF SHARES



Buyer transfers part of its own shares to the seller, and the seller transfers its shares in the target to the buyer

A transaction of this type can be structured as an exchange of shares of the sold company for shares in the buyer (or a subsidiary). For various reasons—admittedly, most often tax considerations (although they can be other reasons, such as giving the buyer the right to elect to make a possible partial "payment" in its own shares)—a more advantageous solution may be the institution known as *datio in solutum*. This is a type of "accord and satisfaction" where the parties agree that the debtor can give something in lieu of a cash payment, discharging the debt (Civil Code Art. 453).

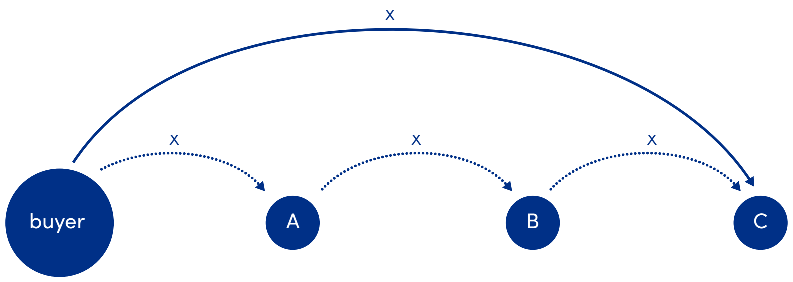
In such case, by transferring the buyer's own shares (or shares in a subsidiary of the buyer) to the seller (with the seller's consent), the buyer discharges its obligation to pay the relevant portion of the agreed purchase price. Such a transfer of shares is thus a substitute for the cash consideration originally agreed by the parties.

Simplification of the payment process on the closing date

One of the thorniest practical issues associated with closings—especially of more complex deals, and above all those with a complicated structure of payments to be executed upon closing—is to ensure that the payments actually occur on the closing date.

Appearances to the contrary notwithstanding, we are writing this article at the start of 2023, not in the early 1990s. We have all grown accustomed to various payments being executed in real time, but unfortunately this is still not the case where large sums are involved and transfers are made from the other side of the globe. This forces the parties to the transaction—and frankly the lawyers drafting the documents under which the whole process will be carried out—to factor in the time that will potentially be required to make the transfers necessary to close the transaction. Thus the payment process should be simplified as much as possible in the given instance.

REMITTANCE INSTEAD OF A CHAIN OF PAYMENTS



Often in practice it is necessary within the payment structure to transfer funds to A, which then should be passed on to B, and from there to C. When everything is supposed to happen on the same day, and A, B and C have bank accounts in different corners of the world (and different time zones), it may seem impossible to coordinate this process.

But that may be only an apparent impossibility. If for example the buyer has an obligation to pay amount X to A, and A should pay X (although on a different legal basis) to B, and B owes the same amount to C, the institution of a remittance (*przekaz*) under Civil Code Art. 921^1 may be applied. In that case (assuming that the conditions in the code for making the remittance are met), the buyer may pay amount X directly to C, thus discharging not only its own obligation, but also the obligations of A and B.

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Clearly, the solutions mentioned above allowing for alternative settlement of the price in M&A transactions do not exhaust the catalogue of solutions used in practice, but in our view these are the most commonly used approaches.

Whether a specific solution can be applied in the given instance must be carefully analysed in each case. This involves not only a legal analysis of the factual situation, but also an examination of the tax consequences of the planned legal construction. There are no universal, one-size-fits-all solutions in this respect, and an approach that worked well in one project may not work in another, and might cause more harm than benefit to the parties.

We have all grown accustomed to various payments being executed in real time, but unfortunately this is still not the case where large sums are involved and transfers are made from the other side of the globe.

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Tax safety of disposals of shares in real estate companies

For many years, the tax laws in Poland have undergone extensive, often controversial amendments. In addition to modifications of existing tax mechanisms, new mechanisms are introduced whose application raises many doubts in practice. Effective as of 2021, one such change is the requirement for a real estate company to act as the remitter of income tax in the event of a disposal of its shares, even though the real estate company is only the subject of the transaction, not a party to it.

Real estate company

To assess whether this rule applies to a transaction, first it is necessary to determine whether the company whose shares are being disposed of meets the definition of a "real estate company." As of 2021, the Corporate Income Tax Act contains two variants of this definition, one applying to entities beginning their activity, and the other applying to existing entities.

The essence of the regulation and the scope of covered transactions

In the case of a transaction involving a disposal of shares in a company, the totality of rights and obligations in a partnership, participation units, or rights of a similar nature, the real estate company is obliged to pay to the account of the competent tax office, as a remitter, an advance tax of 19% on the income earned by the shareholder on this basis, if:

- The party making the disposal is an entity without a registered office or management in Poland, or a natural person not residing in Poland, and
- The subject of the transaction is shares carrying at least 5% of the voting rights in the company, or a totality of rights and obligations carrying at least 5% of the rights to share in the profits of a partnership (not a legal person) or at least 5% of the total number of participation units or similar rights in a real estate company.

The real estate company's obligation to act as remitter and collect 19% advance tax will also arise if one entity makes more than one transaction (e.g. disposal of company shares) within a period not exceeding 12 months, if together the shares carry at least 5% of the voting rights in the real estate company.

A REAL ESTATE COMPANY

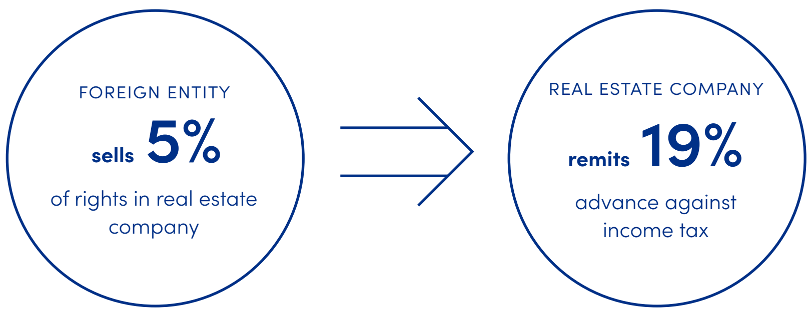
is an entity other than a natural person, required to prepare a balance sheet under the accounting regulations, in which:

Entities beginning their activity	Existing entities
As of the **first** day of the tax year (or financial year when the real estate company is not a CIT payer) • At least **50% of the market value** of the assets directly or indirectly comprises the market value of real estate located in Poland or rights to such real estate, and • The market value of the real estate **exceeds PLN 10,000,000** or equivalent.	As of the **last** day of the year preceding the tax year (or financial year when the real estate company is not a CIT payer) • At least **50% of the carrying value** of the assets directly or indirectly comprises the carrying value of real estate located in Poland or rights to such real estate • The carrying value of the real estate **exceeded PLN 10,000,000** or equivalent, and • In the year preceding the tax year (or financial year), **tax revenues** (or revenues included in the net financial result) from items such as rental, tenancy, financial leasing and other contracts of a similar nature, or from the transfer of ownership, involving real property or rights to real property, and from shares in other real estate companies, **accounted for at least 60% of total tax revenues** (or revenues recognised in the net financial result).

Obligations of the taxpayer and remitter

Pursuant to the CIT Act, the taxpayer, i.e. the entity making the disposal, is obliged to remit the amount of the advance tax payment to the tax remitter before the due date of the advance payment (as a rule, the 20th day of the month following the month in which the income arose). Then, on the date of payment of the advance to the account of the tax office, the remitter must send information to the taxpayer, in compliance with the established template, on the advance payment of tax.

However, the law does not impose an obligation to provide the real estate company with information on the amount of the transaction which would allow it to assess whether the amount transferred by the taxpayer corresponds to the amount of the advance payment actually due. It is only indicated that if the real estate company does not have information on the amount of the transaction, the advance tax is set at 19% of the market value of the shares (or the totality of rights and obligations, participation units or similar rights, as the case may be).



How to understand the concept of disposal of shares?

The CIT Act does not provide a definition of a "disposal." However, there is no doubt that this concept is broader than the concept of a "sale." This position has already been confirmed by the Director of National Revenue Information (e.g. tax ruling no. 0111-KDIB1-2.4010.584.2022.2.AK of 8 December 2022), who has further pointed out that the term "disposal" includes both paid and unpaid forms of ownership transfer.

And recently the first ruling from an administrative court concerning this regulation was issued (Province Administrative Court in Gliwice judgment of 19 December 2022, case no. I SA/Gl 827/22, not final). According to the court, the term "disposal" includes not only bilateral contracts, but can also include for example a unilateral relinquishment of a right.

This means that the types of transactions in which a real estate company has the duty to act as the tax remitter can be very broad in practice.

The holding by the court in Gliwice cited above, regarding application of the new regulation to income received in

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connection with the liquidation of a real estate company, is also worth examining. According to the court, in the case of liquidation of a company, it is possible that income arises on its part, but it is created exclusively by a special provision (Art. 14a of the CIT Act), i.e. income without the occurrence of gain. At the same time, in the court's opinion, the obligation of the real estate company to act as the remitter of the tax should be limited to cases where the taxpayer earns income as understood in the general sense (i.e. arising under Art. 12 or 14 of the CIT Act), as a pecuniary gain of a permanent nature effectively obtained during the tax year.

EXAMPLE **DIVISION BY SEPARATION**

A Polish limited-liability company meets the definition of a real estate company. The company's sole shareholder is a German company. The shareholders of the German company intend to divide the Polish company so that part of its assets constituting an organised part of the enterprise within the meaning of German tax law, including the shares in a Polish real estate company in accordance with the division plan, will be transferred by operation of law to a newly incorporated company under German law.

The Polish real estate company had doubts whether it must act as a remitter and pay advance CIT in connection with the planned division by separation of the German company, which will result in the transfer of its shares by universal succession to a newly established company under German law.

According to the Polish real estate company, the transfer of shares to a newly established company under German law as part of the succession does not fall under this regulation, as no bilateral legal transaction will be concluded involving the transfer of shares in the real estate company.

The Director of National Revenue Information disagreed with the position of the Polish real estate company and pointed out that the transfer of shares by operation of law to the newly established German company constitutes a form of share disposal. The authority determined that income taxable in Poland would arise on the part of the German company being divided, and as a result, the Polish real estate company would be obliged to act as the remitter of the tax.

Tax ruling of 14 September 2022, no. 0111-KDIB1-2.4010.99.2022.2.AW

How to conduct the transaction safely?

Given the above interpretive difficulties and the lack of explicit indication of the transactions in which the real estate company is required to act as the remitter of the income tax, the first step to be taken to secure the tax side of the planned transaction is to determine whether the new regulation may be applied at all. If so, it is then necessary to determine whether the transaction will give rise to income, and consequently whether the real estate company will be required to remit an advance tax payment.

In certain cases, it may be advisable to request a tax ruling and confirm the correctness of the position taken. On one hand, obtaining a tax ruling will protect the taxpayer, as it will confirm the tax consequences of the planned transaction on the taxpayer's side (e.g. whether or not income arises). On the other hand, the real estate company will obtain confirmation that it will correctly act or not act as a remitter in the specific transaction. From the remitter's perspective, obtaining this confirmation can be momentous, since under the Tax Ordinance, a remitter who fails to remit the tax as required is liable for the tax that was uncollected, or was collected but not remitted. In this case, such liability on the part of the real estate company cannot be excluded or limited, even if the tax was not collected through the fault of the taxpayer (i.e. the shareholder disposing of shares in the real estate company).

To ensure the tax security of the transaction, we also recommend including appropriate clauses in the transaction documents (e.g. the share purchase agreement) requiring the parties to provide the real estate company with all documents on the basis of which the amount of the advance tax payment can be calculated.

Summary

According to the explanatory memorandum to the amending act introducing this regulation, shifting the obligation to settle the income tax from the foreign taxpayer to the real estate company was intended to increase the efficiency of income tax collection. This aim cannot be condemned in itself, but introducing a regulation that makes an entity that is not a party to the transaction responsible for collecting the tax on the transaction should be viewed negatively. Additionally, this regulation has been unclear from the very beginning and requires special steps to be taken to prevent negative consequences of erroneous application (or non-application) of the regulation.

Undoubtedly, it is possible to carry out a disposal of shares of a real estate company in a tax-safe manner, but it is necessary to plan the transaction and determine its tax implications well in advance.

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Compliance in public companies: New challenges

Corporate compliance with laws and best practices requires ongoing review of internal procedures. When adapting to new regulations, it is vital to consider the specifics of the company's operations. Lengthy procedures, often simply copying the wording of the regulations, are no help, and when they are hard to understand they may be improperly applied, generating risk of liability for the company and its authorities.

Below we discuss a few new regulations that should be reflected in companies' internal operating rules.

Strengthening the role of the supervisory board

An amendment to Poland's Commercial Companies Code concerning the rights and responsibilities of the supervisory board entered into force on 13 October 2022. These are major changes in light of the provisions of the Public Offerings Act (Act on Public Offerings and Conditions for Introduction of Financial Instruments into Organised Trading and on Public Companies), under which it is possible to punish not only the company and its management board, but also the supervisory board—although previously the supervisory board was not adequately equipped with oversight instruments or access to management information.

Under the amendment, the management board is required to provide information to the supervisory board on the company's current condition and activities, even without first being requested to do so by the supervisory board. The supervisory board should be informed of resolutions adopted, the current asset situation, and other relevant circumstances, including transactions concluded and progress in achieving indicated growth targets. The management board is now required to provide such information at every session of the supervisory board and also promptly after such circumstances arise.

The supervisory board is entitled to examine all documents of the company. It can also demand reports and clarifications from the management board and employees. The requested information must be provided promptly, but within no longer than two weeks. The new regulations expressly prohibit the management board from restricting the supervisory board's access to the requested information, documents, reports or clarifications.

The supervisory board must notify the auditor who examined the financial report of the scheduled session at which the auditor is to present the report on the examination to the supervisory board (including the auditor's assessment of the grounds for adopting a statement on the company's capacity to continue operating), and to respond to questions from the supervisory board members.

A further entitlement has been added authorising the supervisory board to directly appoint an adviser to examine a particular issue without the need to obtain consent from the general meeting or the management board.

The management board can be sanctioned for failing to perform these obligations:

– For failure to timely provide the supervisory board with information, documents, reports or clarifications, or providing inaccurate data or concealing data, a fine of PLN 20,000–50,000 or probation
– For causing the management board not to provide the supervisory board adviser access to documents, not to provide the requested information, to provide inaccurate information, or to conceal data, a fine of PLN 20,000–50,000 or probation.

In light of the provision of the Public Offerings Act on the liability of members of the supervisory board if it is found that the company is not performing its statutory obligations, and the right of the Polish Financial Supervision Authority (KNF) to impose a fine in this respect, it is vital to pay due attention to the organisation of the supervisory board's work, the frequency of sessions, and the manner of documenting its work, which will provide evidence of due diligence on the part of the supervisory board members.

It is worthwhile to introduce a rule of careful documentation of the supervisory board's work, including preparing detailed minutes of sessions and activities, illustrating the manner of performance of the statutory functions of the supervisory board and the activity of specific members. The same applies to documentation of the work of the audit committee functioning within the supervisory board, with respect to the tasks indicated in the Auditors Act.

AML

The Anti–Money Laundering Act sets forth a list of obligated entities which must introduce a procedure specifying the financial security measures to be applied: identification and verification of customers, assessment of the customer's economic relationships, and ongoing oversight. Many public companies have been classified as obligated entities.

This category has been expanded to include businesses providing services of maintaining accounting books and preparing tax statements, providing advice, explanations and opinions on tax or customs law, if that is their principal activity, as well as corporate and trust services. If a company from the group provides such services to a public company, it is an obligated institution and should maintain an appropriate procedure as described in the AML Act.

Activity involving the creation of legal persons, performing the function of

NECESSARY CHANGES TO PROCEDURES	APPLIES TO	REGULATED ISSUES
Supervisory board bylaws **Management board bylaws**	Supervisory board Management board	• Frequency of sessions • Rules for detailed minutes of sessions • Procedure for submitting inquiries to the management board • Procedure for appointing advisers • Rules for responding to inquiries from the supervisory board
Mandatory AML/CFT procedure	Group companies providing bookkeeping, accounting and corporate services	• Rules for risk verification and classification • Security measures applied • Reporting obligations
Whistleblowing procedure	Public companies	• How to report infringements • Who examines reported infringements • What steps are taken to redress infringement • Protection of whistleblowers
Sustainability procedure	Public companies	• Reporting procedure and rules

management board member, providing a registered office or address for such entities, acting as a trustee for a trust, or a person exercising rights to shares for another entity (except for listed companies) is an activity subject to entry in the register maintained by the director of the Revenue Administration Chamber in Katowice. Failure to obtain an entry in the register is punishable with a fine of up to PLN 100,000.

Public companies are not subject to the requirement to register with the Central Register of Beneficial Owners (CRBR), but their subsidiaries are. A recent change to the act extended the deadline for filing with the register or amending an entry from 7 to 14 days.

Whistleblowers

The obligation of public companies to address issues of whistleblowers arises out of various regulations.

Art. 97d of the Public Offerings Act introduces an obligation for a company to maintain a procedure for employees to anonymously report violations of law, procedures or ethical standards to a designated member of the management board (or in specific instances the supervisory board).

Art. 53 of the AML Act imposes on obligated entities a duty to introduce an internal procedure for anonymous reporting by employees or affiliates of actual or potential infringements of the AML/CFT regulations.

The government has published a draft Whistleblowers Protection Act. It provides for an obligation to adopt in an internal procedure a system of incentives to use the internal reporting procedure, when an infringement of law can be effectively handled within the legal entity's organisational structure, and the person reporting the violation believes there is no risk of retaliation.

Crowdfunding

In addition to entry into force of Poland's Act on Social Financing for Commercial Ventures and Aid for Borrowers, another set of provisions governing crowdfunding will be brought to bear on public companies under the EU's Crowdfunding Regulation (2020/1503). The EU regulation applies directly, and thus not all issues covered by the regulation have been carried over into Polish law, but the Polish act cross-references the EU regulation. To obtain a full picture of the regulations, it is essential to examine both laws together.

Crowdfunding services are defined as the matching of business funding interests of investors and project owners through the use of a crowdfunding platform, including for example facilitation of granting of loans and placing of securities without a firm commitment basis. The aim of providing crowdfunding services is to facilitate financing of a project by raising capital from a large number of investors, each of whom invests a small contribution, via a public internet platform, without defining the set of investors.

A company operating a regulated market, as well as any other legal person, may conduct crowdfunding services after obtaining a licence from KNF.

A public offering conducted via a licensed service provider does not require the intermediation of an investment firm, but requires publicising of a key investment information sheet, with prior notification of KNF.

Carrying out a public offering without complying with these requirements is punishable by a fine of up to PLN 10 million, imprisonment of up to two years, or both.

A provider of crowdfunding services must provide KNF with information in the scope and time specified by the minister for financial institutions.

Sustainability

As we signalled in the 2022 *Yearbook*, additional reporting obligations on environmental, social and governance issues have been imposed on Polish public companies via direct and indirect application of EU legislation.

It is crucial to notice that compliance with sustainability principles is inseparably tied to the compliance function. Fulfilment of ESG requirements for the company would not be possible if the company did not operate in compliance with applicable laws and best practices. Moreover, the overriding theme of the concepts of both ESG and compliance is not just managing risks affecting the company, but also identifying and exploiting opportunities.

ESG reporting has become an element of the operation of listed companies due to imposition on them of the duty to include information on ESG issues in non-financial reports. Along with implementation of the EU's Sustainable Finance Disclosure Regulation (2019/2088), the obligation to disclose information on sustainability has been expanded to cover entities providing financial services.

Further changes in this area may involve, among other things, other forms of presenting information, including reports on fulfilment of sustainability criteria.

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Acquisition of a listed company: A big change, but less of a challenge?

Last year, long-awaited changes were introduced to the rules for conducting public tender offers for shares of companies listed in Poland. They have a major impact on acquisitions carried out on the public market, including the transaction structure. It is clear already that the new rules will not make it easier to delist companies.

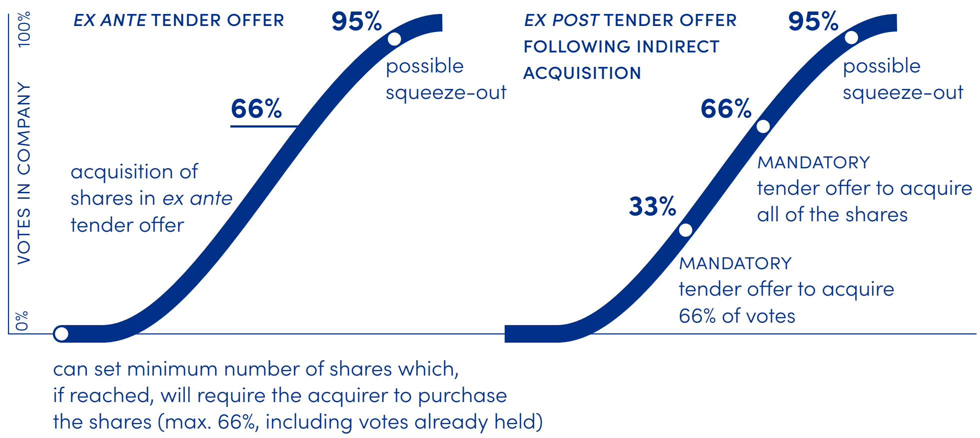
Before the change: two thresholds

The amendment of the Public Offerings Act (Act on Public Offerings and Conditions for Introduction of Financial Instruments into Organised Trading and on Public Companies) entered into force on 30 May 2022. Among other things, the amendment changed the rules for conducting public tender offers for shares in listed companies on the regulated market in Poland.

Previously, an investor who wanted to take control of a listed company had to make a prior (*ex ante*) tender offer for all shareholders to sell their shares in the company. This also applied to shares purchased from a particular seller holding a controlling stake in the shares, who agreed to sell the shares in a prior agreement with the investor. The situation was different in cases where an investor acquired a controlling stake in a listed company indirectly, i.e. bought shares of a company that directly held that stake. Then the investor had to announce a tender offer after already indirectly acquiring a controlling stake in the public company (follow-up (*ex post*) tender offer).

Additionally, the act set two thresholds that triggered the need for a tender offer, at 33% and 66% of the total number of votes in the company. Exceeding the first threshold required the announcement of a tender offer for shares in a number ensuring the achievement of 66% of the total number of votes, and exceeding the second threshold required a tender offer for all the company's shares.

WAS



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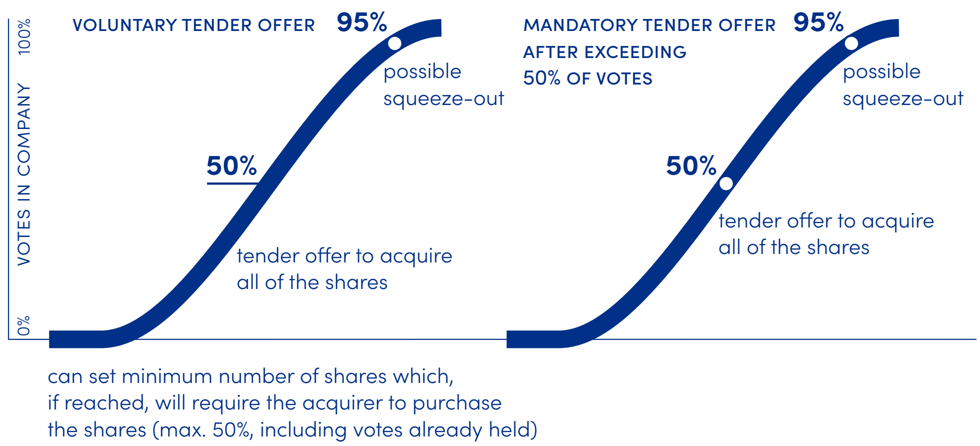

Currently: one threshold for tender offers

The amendment to the Public Offerings Act abolished the previous tender offer thresholds, introducing in their place a single threshold of 50% of the total number of votes in a company. Exceeding it requires announcement of a tender offer for all remaining shares in the company (mandatory tender offer). The rule applies to companies incorporated in Poland or non-EEA incorporated companies which have a listing on a regulated market in Poland.

As a result, an investor can purchase any number of shares directly from one or more shareholders, but if a transaction results in obtaining voting power exceeding 50% of the total votes in the company, the investor will have to announce a public tender offer for the sale or exchange of the company's remaining shares within three months of exceeding the threshold. During that period, the investor cannot purchase shares in the company other than by tender offer. However, the obligation to announce a tender offer does not arise if the threshold of 50% of votes was exceeded as a result of a voluntary tender offer. Like a mandatory tender offer, a voluntary tender offer should be announced for all of the remaining shares (i.e. not held by the bidder) in a public company (tender offers are regulated in Art. 72a–81 and 91 of the Public Offerings Act).

With the exception of a few provisions, most of the regulations on mandatory tender offers apply to voluntary tender offers. However, for voluntary tender offers, the law provides a broader catalogue of conditions precedent that can be stated in the tender offer document, upon fulfilment of which the bidder will be required to buy the shares in the tender offer. Such a condition could be, for example, adoption of a specific resolution by the general meeting or supervisory board of the target company. Similarly, the bidder can specify in the wording of the voluntary tender offer the minimum threshold of shares declared by shareholders for sale in the tender offer, after reaching which the investor will be obliged to purchase shares in the tender offer (minimum acceptance threshold). Significantly, the minimum acceptance threshold in a voluntary tender offer, which includes shares already held by the investor, cannot be set at a level exceeding 50% of the total number of votes in the company's general meeting (before the amendment, the threshold could be set at a maximum of 66% of the total votes in the case of *ex ante* tender offers, which corresponded with the higher tender offer threshold in force at the time).

In market practice, a frequent motive for taking over listed companies is the desire to delist the company's shares from the regulated market. This requires a decision of the company's general meeting adopted by a nine-tenths majority of votes cast in the presence of shareholders representing at least half of the share capital. For practical reasons, investors intending to take the company private expect delisting to occur when they are the only remaining shareholder in the company. This in turn is made possible by a squeeze-out procedure » for minority shareholders, for which 95% of the total votes in the company is required (Art. 82 of the Public Offerings Act).

The possibility of setting the minimum threshold of shares to be purchased in the wording of the tender offer at a high level, and preferably at a level allowing for compulsory buyout of minority shareholders, is an important criterion to be taken into account by investors deciding to pursue the takeover of a public company with a plan to subsequently delist it (although this is not always the case, as investors may be interested in keeping the company on the exchange after taking control of it).

However, if the purpose of the acquisition is to take the company's shares out of public trading, an investor will be expected to be less inclined to launch a public tender offer if the risk of obtaining a stake below the squeeze-out threshold is significant. The spread between the threshold of 50% and 95% of votes is wide, and the provisions allowing the minimum acceptance threshold in a voluntary tender offer to be set at 50% of the votes do not make it easier for investors. Moreover, lowering this threshold from 66% to 50% of voting rights increases the risk that investors will be less willing to attempt to take over listed companies, and as a result, it will be more difficult to withdraw a company from public trading.

Lowering this threshold from 66% to 50% of voting rights increases the risk that investors will be less willing to attempt to take over listed companies, and as a result, it will be more difficult to withdraw a company from public trading.

How does it work in practice?

We can analyse the application of the amended regulations with an example. An investor is considering taking control of a Polish company listed on the regulated market operated by the Warsaw Stock Exchange with the intention of delisting its shares from the WSE. About 45% of the company's shares are in the hands of one major shareholder who wants to sell his shares to the investor, while the remaining shares are in free float.

Seeking to take control of the company and have the shares delisted, the investor intends to launch a voluntary tender offer for shareholders to sell all of the company's shares. Prior to announcement of the tender offer, the investor agrees with the major shareholder on the terms of the sale of his 45% stake.

Bearing in mind the purpose of the transaction, the investor would like to safeguard its interests and indicate in the tender offer that it will be obliged to purchase shares from shareholders responding to the tender offer only if it secures the threshold of 95% of the voting rights, enabling it to carry out a squeeze-out. Unfortunately, as pointed out above, the provisions on tender offers prohibit the investor from setting the minimum acceptance threshold at higher than 50% of the company's voting rights. Nevertheless, the investor decides to go ahead with the transaction.

After agreeing with the major shareholder that he will sell his stake to the investor in the tender offer, the investor announces a tender offer and the major shareholder responds to the tender offer with respect to all of the shares he holds (i.e. 45% of total votes). The investor then anxiously waits to see if it will obtain the missing 50% of shares (45% + 50% required to reach the 95% threshold allowing a squeeze-out) in the tender offer from the other shareholders in the free float. But this solution is quite risky, as one of the goals of the transaction was to acquire 100% of the shares and delist the company. The investor is left to encourage shareholders to sell their shares by increasing the proposed price, but even this does not guarantee the intended effect.

In this example, the investment was not fully successful, as the investor achieved a total of 70% of the company's shares in the tender offer, so the company will remain on the trading floor for some time to come.

Could the investor have structured the transaction differently to reduce these risks? It seems so. However, this would require reversing the order of the bundles of shares to be acquired, so that when subscriptions for a predetermined number of shares are received from shareholders in the free float, the major shareholder's bundle steps up to, as it were, "close" the tender offer.

The introduction of a single threshold for tender offers announced in connection with takeovers of public companies and the division of tender offers into mandatory offers and voluntary offers make the legal mechanisms governing them more transparent. However, linking the minimum acceptance threshold, as a condition for acquiring shares in a voluntary tender offer, with the mandatory tender offer threshold of 50% of voting rights, means that investors interested in acquiring full control of a company must continue to face challenges.

We will be curious to see how the market adapts, and assess the operation of these legal solutions for tenders to take over listed companies.

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Binding instructions within corporate groups

Under Polish law, parent companies have recently been allowed to issue binding instructions to their subsidiaries. With this change, parents and subsidiaries can be guided by a shared economic strategy to further the interests of the corporate group. But when must a subsidiary execute binding instructions?

A major amendment to the Commercial Companies Code, passed on 9 February 2022, entered into force on 13 October 2022. It established the rules for functioning of corporate groups in Poland and modified certain regulations governing company authorities.

The aim of the changes

This amendment to the Commercial Companies Code is one of the most important changes in Polish corporate law in the last two decades. It is aimed at systematically regulating the operation of corporate groups, which before had been subject only to general regulations.

The absence of specific statutory provisions meant that in conducting the affairs of a subsidiary, it was hard to take into account the interest of the group, if that interest diverged from the interest of the subsidiary within the group. The previous regulations required the authorities of a company to act solely in the best interest of the company, and provided no immediate grounds to take into account the interest of the group in pursuing the subsidiary's affairs. This situation was partially mollified by the rulings of the commercial courts, holding that the interest of the group is part of the broadly defined interests of the company.

The amendment to the code was designed to allow the parent company and the subsidiaries to be guided by a common economic strategy with the aim of pursuing the interests of the group of companies.

To achieve this aim, various instruments were introduced into the code for the authorities of the parent company to exercise uniform control over subsidiaries, such as:

- Entitlement of the bodies of the parent company to exercise ongoing supervision over implementation of the interests of the group by the subsidiary
- The absolute and unlimited right of the parent company to access information about the affairs of the subsidiary
- The right of the authorities of the subsidiary to take into account the interests of the corporate group in conducting the affairs of the subsidiary
- The institution of binding instructions issued by the parent company with respect to the manner of conducting the affairs of the subsidiary.

The members of the subsidiary's authorities will not be liable for injury caused to the company if they acted in the interest of the group in executing a binding instruction. Along with these changes, special free-standing rules were introduced providing for the parent company's liability for injury to the subsidiary resulting from execution of binding instructions, as well as liability in this situation for injury caused by the parent company to the creditors or minority shareholders of the subsidiary.

The institution of binding instructions lies at the foundation of the newly introduced solutions. But it is worth considering whether binding instructions can be helpful in exercising uniform control over the affairs of subsidiaries and whether this institution is capable to achieving the aims sought by lawmakers in drafting these changes to the law.

Possibility of issuing binding instructions

The parent company may issue binding instructions to a subsidiary participating in the group concerning the manner of conducting the subsidiary's affairs, if justified by the interests of the corporate group and not otherwise provided by specific regulations. In all these instances, if under separate regulations the company belonging to the group has a duty to pursue a specific aim, for example the statutory duties imposed on public-benefit companies, rather than just the interest of the subsidiary itself and its immediate stakeholders, then the binding instruction cannot be followed. The same applies to binding instructions whose performance would constitute a prohibited act under mandatorily applicable provisions of law.

Issuance of a binding instruction requires written form, or electronic form using a qualified electronic signature, in either case under pain of invalidity. On the part of the subsidiary in the group, execution of a binding instruction requires adoption of a prior resolution of the subsidiary's management board. The subsidiary must promptly inform the parent company of adoption of the resolution.

Significantly, the Commercial Companies Code allows for issuance of binding instructions only when a formal corporate group has been established. A corporate group in this sense will arise only when resolutions have been adopted by the shareholders meetings of the subsidiaries on membership in the group, and formation of the group is disclosed in the commercial register.

Under the newly introduced provisions of the Commercial Companies Code, the subsidiary may refuse to carry out the binding instruction only when executing the instruction could render the company insolvent or expose it to a danger of insolvency. Refusal to carry out a binding instruction requires adoption of a resolution by the management board of the subsidiary. Subsidiaries that are not wholly-owned may refuse to carry out a binding instruction also if it gives rise to a justified concern that the instruction is contrary to the interests of the subsidiary and will cause injury to the subsidiary that cannot be redressed within two years.

It appears that the authorities of the subsidiary must examine in each instance:

- Whether issuance of the binding instruction is consistent with the interests of the corporate group to which the subsidiary belongs
- Whether the binding instruction infringes statutory duties imposed on the subsidiary and is lawful
- Whether there are factual grounds for refusing to carry out the binding instruction arising out of the Commercial Companies Code.

Under the new regulations, the subsidiary's articles of association may introduce additional conditions restricting the possibility of refusing to carry out binding instructions. Typical added conditions include a quorum requirement or obtaining a heightened majority of votes when adopting a resolution of the subsidiary's management board refusing to carry out a binding instruction.

The members of the subsidiary's authorities will not be liable for injury caused to the company if they acted in the interest of the group in executing a binding instruction.

Issuance of a binding instruction requires written form, or electronic form using a qualified electronic signature.

Only after verifying that there are no grounds for refusing to carry out a binding instruction can the management board of the subsidiary lawfully adopt a resolution on execution of the binding instruction. Maintaining the required due diligence will enable the management board of the subsidiary to be relieved of liability for injury suffered by the subsidiary arising out of the actions by the management board pursuing the interests of the corporate group based on binding instructions received from the parent company.

The nature of binding instructions

The amendment to the Commercial Companies Code does not contain any provisions expressly recognising the existence of liability on the part of the subsidiary's management board for failing to carry out a binding instruction when there are no grounds or legal bases for refusing to carry it out.

It should nonetheless be recognised that a binding instruction is a unilateral legal act by the management board of the parent company, shaping the corporate-law relations associated with serving on the management board of the subsidiary. In effect, groundless refusal by the subsidiary's management board to carry out a binding instruction from the parent exposes the management board members to liability for a tortious act if it results in injury to the parent company or another company in the group arising from the failure to act.

Rules for liability for injury caused by binding instructions

The amendment to the Commercial Companies Code imposes on the parent company the duty to act with loyalty towards the subsidiary in connection with issuance and execution of binding instructions. However, the code does not define how the duty of loyalty related to binding instructions should be understood. It should be recognised that action will be deemed loyal only if it involves:

- Provision by the parent to the subsidiary of complete information on the circumstances associated with the binding instruction, including the anticipated consequences of execution of the binding instruction for the subsidiary carrying out the instruction and other companies in the group
- Introduction of realistic mechanisms for redressing the injury caused by execution of the binding instruction within the time allowed for making up the loss.

The amended code provides that in the event of failure to act in compliance with the principle of loyalty, the parent company shall be liable for the injury to the subsidiary connected with issuance or execution of the binding instruction. It appears that the substance of the duty to act loyally will be determined by the possibility of ascribing fault to the parent company in holding it liable in tort for the injury to the subsidiary.

The lawmakers also created a basis for the parent company's liability to the minority shareholders of the subsidiary for the indirect injury suffered by them in the form of a decline in value of the shares in the subsidiary held by the minority shareholders, if the injury resulted from issuance of a binding instruction to the subsidiary. The minority shareholders carry the burden of proving injury on their part and a causal connection between the binding instruction issued to the subsidiary and the injury. The parent company's liability for indirect injury to the minority shareholders of the subsidiary is apparently the first example of establishing a statutory basis for liability of this sort, which in certain instances was previously inferred in the form of a duty to redress injury under general provisions of law, via the case law of the commercial courts.

If enforcement against the subsidiary is ineffective, a creditor of the subsidiary will be able to seek satisfaction of its claim against the parent company, unless the parent company shows that it was not at fault or that the injury did not result from execution by the subsidiary of a binding instruction. The new regulations, operating on the basis of legal presumptions, will allow the parent company to be held liable for unsatisfied obligations of the subsidiary only based

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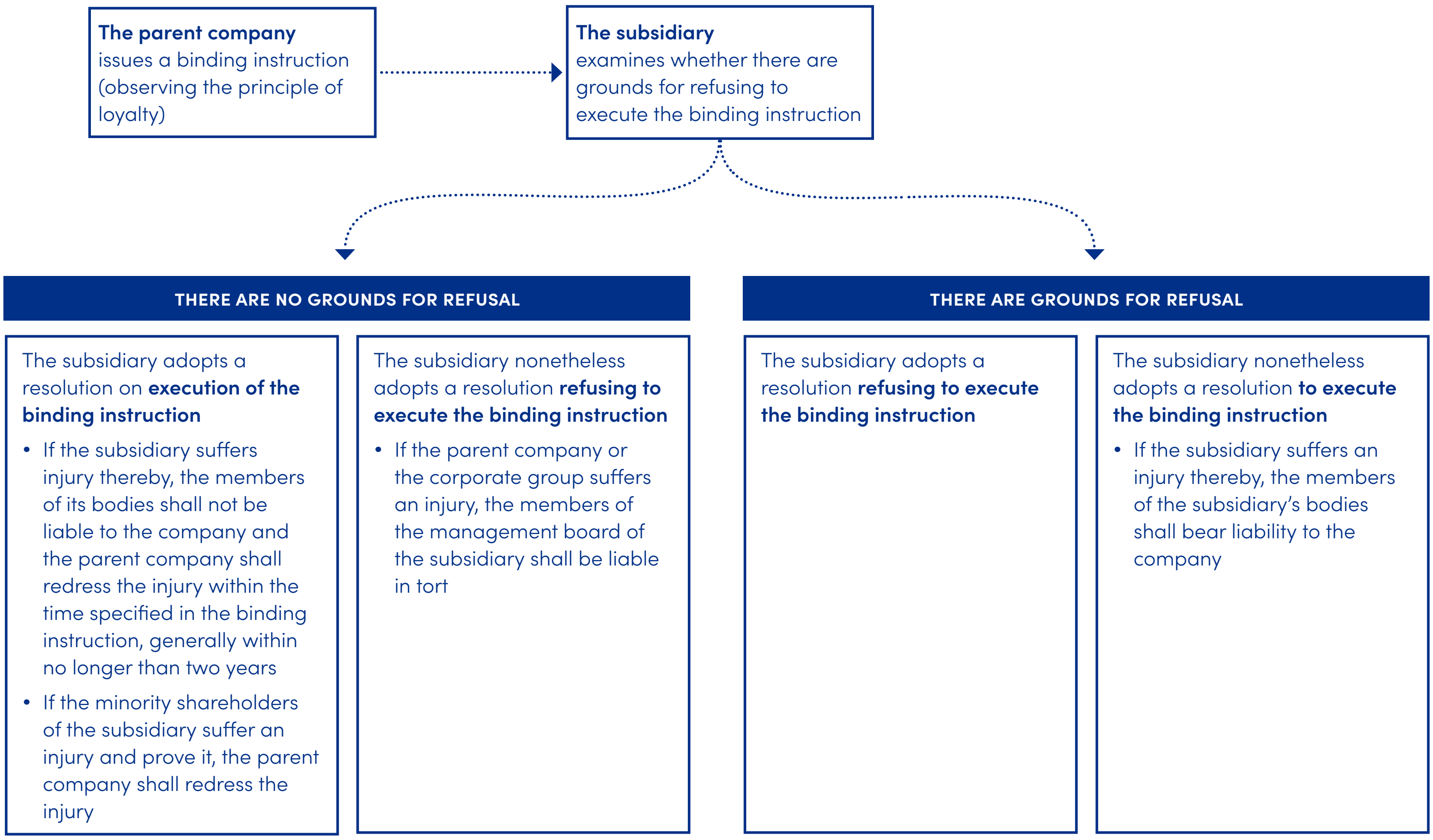
Only after verifying that there are no grounds for refusing to carry out a binding instruction can the management board of the subsidiary lawfully adopt a resolution on execution of the binding instruction.

FORMAL CORPORATE GROUP



on proof supplied by the creditor that the subsidiary carried out binding instructions during the relevant time and was not in a position to satisfy its obligations. This evidence will not be difficult to produce, as the essential circumstances are subject to disclosure by the companies participating in the group. It should be assumed that the situation of parent companies with respect to their liability to creditors of the subsidiary will be essentially the same as the situation of the members of the management board of the subsidiary with respect to unsatisfied obligations of the subsidiary.

Are binding instructions a useful legal instrument for parent companies?

It seems that the institution of binding instructions may be a convenient tool in cases where it is necessary to act in the interests of the corporate group contrary to the interests of the subsidiary. Such a need often arises in corporate operations. It is unfortunate, however, that lawmakers did not specify in sufficient detail the consequences of failure to execute binding instructions when there are no grounds for refusing to carry them out. It is also too bad that the law limits the liability of the parent company for injury to the subsidiary, its creditors, or minority shareholders exclusively to instances of issuance of formal binding instructions within a formally established corporate group.

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Can shareholders or partners compete with their own company or partnership?

The answer largely depends on how this issue is regulated within the specific corporate entity. It is even more complex if the members did not include relevant contractual provisions at the stage of formation of the company or partnership. The issue is handled differently in partnerships, where the element of mutual trust and cooperation between partners is considered vital, and in companies, where direct management of the company's affairs is exercised by members of the management board, and it is the management board members who are subject to a statutory ban on competition.

The question in the title might arise in a hypothetical situation where two manufacturing companies entered into a joint-venture agreement and subsequently established a limited-liability company for the purpose of implementing the joint venture. In the joint-venture agreement, there was a ban on competition expressly referring to only one shareholder, specifying which activities that shareholder was not allowed to engage in. The other shareholder was not subject to an express contractual ban on competition.

After a while, it became apparent that the production was not meeting the customers' quality requirements, and this gave rise to a conflict between the shareholders. The shareholder who was not subject to an express ban on competition then set up a new company and began producing competing products—admittedly with a slightly different composition, but from the same market segment. As a result, the other shareholder accused the enterprising shareholder of violating the principle of loyalty to the company, and sought to hold it liable for injury allegedly suffered by the company and the other shareholder.

Under Polish law, situations of this type should be analysed in relation to partnerships (*spółki osobowe*) and companies (*spółki kapitałowe*), as there are fundamental differences.

Competition by partners

In partnerships, the partners (or some of them) have the right and duty to manage the partnership's affairs. As a result, a ban on competition pertaining to partners is explicitly provided for in the Commercial Companies Code. Pursuant to Art. 56, in a general partnership (*spółka jawna*),

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Each partner in a general partnership has the right to demand disgorgement to the partnership of benefits obtained by a partner in breach of the prohibition on competition, or to redress damage caused to the partnership.

a partner is obliged to refrain from any activity conflicting with the interests of the partnership and, without the express or implied consent of the other partners, may not engage in a competitive business, in particular by participating in a competing entity as a partner in an ordinary partnership (*spółka cywilna*), a partner in a general partnership or professional partnership (*spółka partnerska*), a general partner in a limited partnership, or a member of the governing body of a company or partnership. Commencement of independent business activity by a partner of a general partnership, where the subject of the business overlaps with that of the partnership, also violates the ban on competition referred to in Art. 56 of the Commercial Companies Code (Supreme Court of Poland judgment of 20 August 2015, case no. II CSK 505/14).

Art. 57 of the code provides that each partner in a general partnership has the right to demand disgorgement to the partnership of benefits obtained by a partner in breach of the prohibition on competition, or to redress damage caused to the partnership. These claims become time-barred six months from the date when all other partners became aware of the violation of the ban, but no later than three years. Violation of the ban on competition also constitutes valid grounds to order the exclusion of a partner from the partnership at the request of the other partners.

The provisions on general partnerships apply as relevant to other partnerships under the Commercial Companies Code, which means that the ban of competition applies to the partners or members of the management board authorised to conduct the partnership's affairs or represent the partnership. However, this ban does not apply to limited partners in a limited partnership (*spółka komandytowa*), based on Art. 121 §3, which provides that restrictions on competitive activities do not apply to a limited partner who does not have the right to manage the affairs of the partnership or represent it, unless the partnership agreement provides otherwise. Similarly, in the case of a joint-stock limited partnership (*spółka komandytowo-akcyjna*), the ban on competition applies only to partners, not shareholders (Art. 126 §1(1)).

6 MONTHS

Limitations period on claims for infringement of ban on competition, counted from the date when all partners learned of the infringement

Therefore, it should be borne in mind that where the role of a partner in a partnership is similar to that of the management board in a company, the restrictions on the competitive activities of partners are similar to those of members of the management board of companies.

The partnership agreement may also clarify or expand the ban on competition beyond the code provisions, as well as extend its duration for a specific period after a partner leaves the partnership.

Competitive activities of shareholders in companies

Unlike members of partnerships, with regard to shareholders of companies there is no ban on competitive activities explicitly provided for in the Commercial Companies Code. However, some commentators argue that such a restriction on shareholders can be inferred from the duty of loyalty to the company, understood as the duty to act honestly and in good faith, as well as the duty provided for in Art. 3 of the code to pursue a common goal, and thus also to refrain from competing with the company.

However, the question arises whether a general duty of loyalty to the company can lead to the conclusion that a shareholder must refrain from activities competitive with the company.

In the case of a limited-liability company (*spółka z ograniczoną odpowiedzialnością*) and a joint-stock company (*spółka akcyjna*), a ban on competition is expressly provided for members of the management board, and in a simple stock company (*prosta spółka akcyjna*) also for the members of the board of directors. Therefore, a management board member or director cannot, without the company's consent:

- Handle the affairs of competitors
- Participate in a competing entity as a partner in a partnership or as a member of a corporate body of a company
- Participate in another competing legal person as a member of a corporate body, or
- Participate in a competing company, if the person holds at least 10% of the shares in the competing company or the right to appoint at least one member of its management board.

PROHIBITION OF COMPETITION IN POLISH COMPANIES AND PARTNERSHIPS UNDER THE GENERAL RULES OF THE COMMERCIAL COMPANIES CODE

	PARTNERSHIPS				COMPANIES		
	general partnership (sp. j.)	professional partnership (sp. p.)	limited partnership (sp. k.)	joint-stock limited partnership (SKA)	limited-liability company (sp. z o.o.)	joint-stock company (SA)	simple stock company (PSA)
COVERED BY BAN	all partners responsible for conducting the partnership's affairs or representing the partnership		general partners		management board members		members of management board or board of directors
NOT COVERED BY BAN			limited partners	shareholders	shareholders		

But there is no analogous provision expressly requiring shareholders of a company to refrain from competitive activity. Deriving a duty to refrain from competitive activity from the mere fact of being a shareholder in a company is dubious, as Polish law does not explicitly indicate such an obligation. And if there is no explicit obligation on the part of the shareholders to refrain from activity competitive to the company, such action cannot be alleged to be unlawful. If the parliament really wanted to extend a ban on competition to shareholders of companies, it would have done so explicitly, as it did for management board members.

The position of the Supreme Court

In considering this issue, the Supreme Court of Poland has taken the position that a ban on competitive activities may arise either by law or by agreement. The Commercial Companies Code imposes some sort of non-competition in every type of company or partnership, but the subject matter and persons covered by such a ban vary depending on the type of company or partnership. The set of persons covered by the ban on competition is broadest in partnerships, as it includes all partners responsible for managing the partnership's affairs and representing the partnership. In companies, the statutory ban on competitive activities does not apply to shareholders, but only to members of the management board, although even this is not absolute, as it can be lifted by obtaining the company's consent. The Supreme Court has also pointed out that the set of persons covered by the ban on competition may be expanded from that provided in the code by including in the articles of association an express obligation to refrain from competitive activities, even extending to all shareholders, if this is their intention and it is justified by the circumstances of the specific company (Supreme Court judgment of 18 April 2018, case no. IV CSK 352/17).

In the justification for that judgment, the court indicated that the introduction of a ban on competitive activities not originally provided for in the articles of association constitutes an increase in the consideration provided by the shareholders within the meaning of Art. 246 §3 of the Commercial Companies Code, which in practice means that the consent of all shareholders affected by the change must be obtained. In other words, adoption of a resolution introducing a ban in the articles of association on competitive activities by shareholders requires their consent; otherwise, a shareholder can request the court to set aside the resolution.

But the court also stated that the formal absence of a ban on conducting competitive activities does not deprive the company of protection against a shareholder's behaviour constituting a breach of loyalty to the company, which requires shareholders to refrain from actions contrary to the company's interests.

The formal absence of a ban on conducting competitive activities does not deprive the company of protection against a shareholder's behaviour constituting a breach of loyalty to the company, which requires shareholders to refrain from actions contrary to the company's interests.

What does competition law have to say?

An example of behaviour described in the last paragraph is a shareholder's engagement in competitive activity using confidential information or data constituting trade secrets of the company or partnership, obtained in connection with participation in the entity. Such an action may constitute an act of unfair competition banned by Art. 12 and 23 of the Unfair Competition Act. These regulations apply to both partners and shareholders.

However, there is more to a shareholder's or partner's competitive activity than just injury to the company or partnership. Such activity can strengthen market competition, benefitting both customers and the public interest. Competition law protects the mechanism of fair competition by banning agreements that restrict competition. In the case of partnerships, the ban on competitive activities extends by operation of law to all partners responsible for managing the partnership's affairs and representing the partnership. Thus, in a sense, the parliament has recognised that competition between a partnership and such a partner is not fair competition and as such is not protected by law.

The situation is completely different for companies. As the Commercial Companies Code does not expressly ban shareholders from engaging in activities competitive with the company, the Competition and Consumer Protection Act, in particular Art. 6, will be fully applicable to the evaluation of such a ban. It follows from this provision that, in principle, an agreement between business entities (thus this provision does not apply to a shareholder who is not also a business entity) with the purpose or effect of preventing those businesses entities from competing with each other is banned. Thus, establishing a ban on competition between a company and its shareholder (who is also a business entity) violates competition law—subject to certain exceptions, the most important of which are the following.

First, the ban on competition between a shareholder who is a business entity and the company itself is permissible in a situation where the shareholder sells its shares to a new purchaser (to the extent specified in the European Commission's Notice on restrictions directly related and necessary to concentrations, 2005/C 56/03).

Second, if the company and a competing shareholder are in a vertical relationship with each other (e.g. supplier and distributor), a ban on competition is permissible to the extent specified in the Regulation of the Council of Ministers of 30 March 2011 Excluding Certain Types of Vertical Agreements from the Ban on Agreements Restricting Competition.

Third, a ban on competition may be permissible if it meets the four conditions set forth in Art. 8 of the Competition and Consumer Protection Act, which in short means that it must bring more benefit than harm to the broader market and competition on the market.

Summary

Partners who manage the affairs of a partnership or are authorised to represent the partnership have a duty to refrain from activities competitive with the partnership.

In companies, by contrast, there is no such obligation for shareholders, unless expressly provided in the articles of association or in a separate shareholders' agreement (as is sometimes the practice). Therefore, a ban on competition should not be inferred from the shareholders' duty of loyalty to the company, all the more so if in an agreement between shareholders, as in the hypothetical described at the outset, this ban expressly applies to only one of the shareholders.

A situation where the shareholder's activity may qualify as an act of unfair competition is a separate issue, as then, for obvious reasons, the shareholder may be held legally liable on this account. It should also be remembered that introduction of a ban on competition between a shareholder who is a business entity and the company is prohibited by Art. 6 of the Competition and Consumer Protection Act, although the act does provide for exceptions.

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How to prepare for implementation of whistleblower regulations?

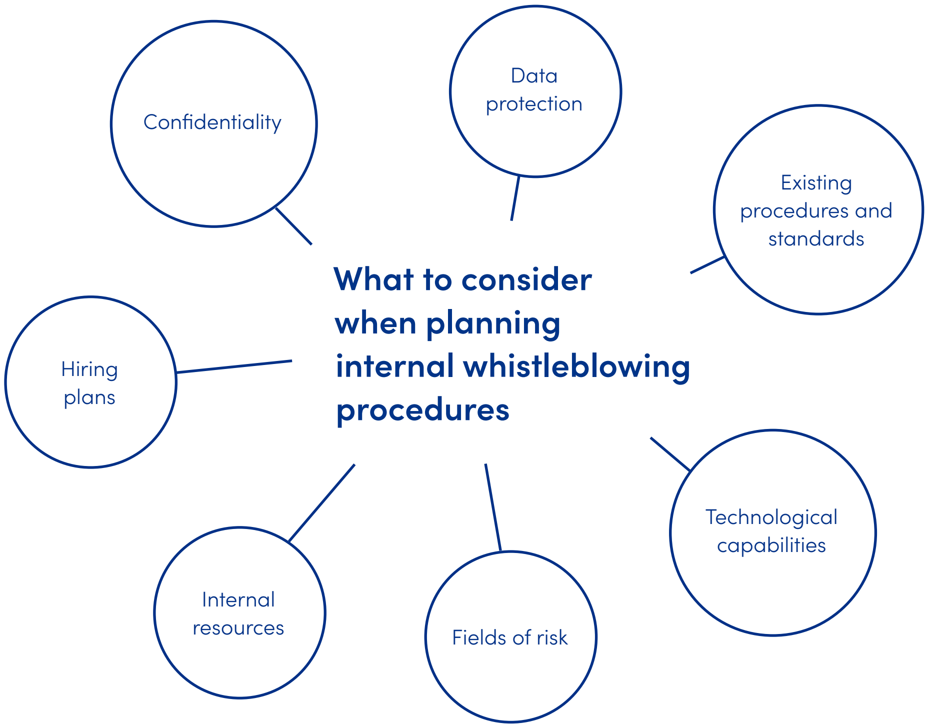
The deadline has passed, but the regulations are not yet in place. Businesses should take advantage of the delay to think through all aspects of their internal whistleblowing procedures.

The deadline for implementation of the EU's Whistleblowing Directive (2019/1937) passed over a year ago, but regulations implementing the directive into the Polish legal system have yet to be adopted. Over the course of the year successive drafts were circulated, but it is hard to resist the impression that the pace of work on the side of the government has slowed to a crawl.

Although the final wording of the Polish regulations is not yet known, it is worth considering the key issues in due time from the perspective of future compliance. This is particularly important in the case of undertakings employing 250 or more people, which will be first group required to implement internal whistleblowing procedures.

Private entities employing 50–249 people will have more time to implement whistleblowing procedures, but the deadline is still fast approaching (under the directive, the deadline for this group of undertakings is 17 December 2023).

In this article we discuss the main areas for functioning of internal reporting channels which require organisations to take implementation decisions, and which they can already start considering.



What will be reported?

All indications are that entities implementing whistleblowing procedures will be able to expand the set of infringements that can be reported to include not just breaches of EU law as referred to in the directive, but also infringements of internal regulations or ethical standards in force within the organisation. This possibility has been included in all drafts so far of the act implementing the directive into Polish law.

However, the decision to include infringements of internal rules and ethical codes in the whistleblowing system should be carefully considered, as such complaints will require follow-up and internal proceedings under the same rules as infringements in other areas.

So it is worth analysing the enterprise's internal procedures and ethical codes now in light of the matters regulated there, as well as the level of detail of these rules. Often ethical codes define standards of behaviour in many areas, and the standards are often vague and general, and thus can be hard to enforce in practice.

At the same time, ethical codes in force at businesses often contain provisions banning discrimination and mobbing. So if they are included in the whistleblowing procedure, the internal reporting channels can morph into a tool for considering individual complaints by employees and associates. This in turn will require businesses to commit greater human and operational resources to consideration of such complaints. Meanwhile, many employers have already implemented separate anti-mobbing procedures. Therefore, before deciding on the areas to be covered by the whistleblowing procedure, employers must also review their internal anti-mobbing procedures and adjust them accordingly (which sometimes may mean having to repeal them entirely), to avoid any conflict in the internal standards at the organisation in this respect.

Who will receive complaints?

A basic challenge for companies is to ensure that the reporting channels function efficiently, and ensure independence and confidentiality. How these channels function will depend on whether people with knowledge of irregularities—potential whistleblowers—decide to report them.

Businesses may designate an internal unit or person within the entity's own organisational structure to receive complaints. However, the directive permits delegation of the duty to receive reports to external entities via outsourcing. Such third parties designated to receive complaints may be providers of tech platforms and solutions for submitting complaints, external advisers, auditors, or even employee representatives.

The decision to use the organisation's own channels or external reporting channels should be preceded by an analysis of the organisation's own capabilities and resources (particularly personnel), the tech solutions and tools offered on the market and the related costs, as well as the additional obligations and risks associated with delegating these tasks to external providers.

External entities hired to handle whistleblowing systems must have appropriate security measures in place and meet certain requirements, in particular involving protection of the safety and confidentiality of whistleblowers and persons identified in the report, as well as protection of other data included in the report, against unauthorised access.

Delegation of receipt of whistleblowing reports to an external organisation will require conclusion of an agreement with the external service provider, and compliance with a range of duties under the regulations on protection of personal data. Businesses must remember in this regard that they bear responsibility for potential breaches by the external entity receiving whistleblower complaints. In particular, it is worth considering securing issues related to violation of confidentiality by including appropriate contractual penalties in the contract with the external service provider.

Which tech solutions?

Under the directive, whistleblowing channels must allow complaints to be made in writing or orally, but it is up to the organisation to decide which type of channel to establish.

Written complaints may be made in traditional or electronic form (e.g. by email). It is also worth considering the possibility of using other tech tools and solutions, e.g. systems specially created for this purpose or various types of messaging services available on the market.

In turn, oral reporting may be done by telephone or other voice communication systems. It should be considered whether the hotline for whistleblowers will be accessible around the clock or only during scheduled hours. While written complaints, particularly in electronic form, can easily be submitted at any time, it will be harder for businesses to ensure constant access to personnel receiving telephone calls from whistleblowers. It would seem to be simpler to use other voice communication systems, such as voicemail, which by their nature do not require the involvement of individuals receiving complaints live in real time.

At the request of the whistleblower, there should also be an option to receive the report via a face-to-face meeting scheduled within a reasonable time. This seems like an attractive form to use, as it allows whistleblowers to present evidence to back their claims, and when needed, for the organisation to clarify certain issues via dialogue between the whistleblower and the person receiving the complaint. But for businesses this will require training of individuals receiving complaints in this form.

Who will follow up?

When a complaint is made, that is the first step, setting off the whole procedure for internal reporting. The next stage (after confirming to the whistleblower that the complaint has been received) is to take follow-up actions. These are aimed at assessing the truth of the allegations raised in the report, and if the breach has not yet occurred, to respond and prevent the breach from occurring.

The next challenge to be met by private entities is thus to designate an individual or unit for taking follow-up actions in connection with a complaint. Selection of the most appropriate person or persons will be determined by the organisation's own structure, the sector in which it operates, and the scale and type of potential breaches. It is worthwhile to identify at the start the risk factors and areas relevant to the organisation's business profile. For example, in the case of entities from the banking sector, a potential risk area would include the assessment of customers' credit capacity and lending decisions, a stage where internal or external pressure might be brought to bear.

In any case, the person designated to take follow-up measures should provide assurances of impartiality, independence, and freedom from conflicts of interest.

It should be pointed out that persons designated to receive complaints may also conduct the follow-up.

Channels for reporting and verification—the organisation's own, or shared?

Entities from the private sector employing 50–249 workers may also decide whether they wish to use exclusively their own in-house channels for reporting and follow-up, or share such resources with other entities. The directive allows this group of entities to create shared channels for receiving reports and conducting investigations. This sharing of resources requires a separate agreement between the entities involved.

Creation of shared channels for reporting and investigation may be particularly suitable for corporate groups where a common hotline or even an entire compliance division examining internal complaints is nothing new, but has been rooted in the corporate culture for a long time. Such solutions are often dictated by the need to ensure consistent standards across the entire group.

Significantly, the directive does not exclude the possibility of creating and using cross-border channels for reporting and follow-up. But the use of international reporting channels may pose serious practical difficulties, primarily arising from the different regulations governing

At the request of the whistleblower, there should also be an option to receive the report via a face-to-face meeting scheduled within a reasonable time.

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Entities employing 250 or more workers are not allowed to use shared resources for reporting and investigation.

whistleblowing procedures at the national level. A separate question is the duty to ensure that the operation of a shared hotline and investigative resources by one (common) entity complies with the data protection regulations. The proposed provisions on this issue in the draft Whistleblower Protection Act in Poland raise many doubts (beyond the scope of this article).

In considering the possibility of using shared channels for reporting and investigating complaints, businesses must take into account the number of employees and associates, as well as planned changes in this regard. Entities employing 250 or more workers are not allowed to use shared resources for reporting and investigation. Thus a rapidly growing enterprise may be able to use shared resources only for a short time, so efforts to arrange shared resources in such cases may not make sense.

Summary

Advance consideration of the model for the internal reporting procedure within the company will allow for efficient implementation of the procedure and completion of other related formalities (including under data protection rules) when the Polish parliament gets around to adopting regulations on whistleblower protection. Well-thought-out and well-functioning procedures should encourage people with knowledge of potential violations to come forward and report breaches.

Smooth adoption of an internal reporting procedure will also allow more time for training people responsible for receiving complaints and conducting follow-up. This in turn will help ensure compliance with the regulations and investigation of complaints in accordance with principles of independence and confidentiality, and protection of both whistleblowers and the persons mentioned in complaints, thus limiting the business's exposure to claims by the persons concerned.

 

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Tightening of advertising rules for regulated healthcare products

Manufacturers of drugs, medical devices, and dietary supplements engage in intense marketing, but are facing ever more far-reaching restrictions on advertising their products. Communications with doctors, patients and consumers of health-promoting products are subject to numerous and rapidly changing legal restrictions. Where to draw the line between advertising bans and restrictions and the right to information about health-related products? And who will be allowed to appear in commercials?

So many products, so many regulations

The advertising of health-related products such as medicinal products (drugs), medical devices and dietary supplements is subject to three separate legal regimes at both the EU and Polish levels.

The tightest restrictions apply to drug advertising. They are provided for in the Pharmaceutical Law of 6 September 2001. For example, pursuant to Art. 57(1), it is prohibited to advertise to the public about medicinal products issued exclusively by prescription.

As for the advertising of medical devices, chapter 12 of the Medical Devices Act of 7 April 2022 devoted to this issue came into force on 1 January 2023.

While rules for advertising and promoting dietary supplements have not been codified, the rapid growth of this market and the significant participation of the media in marketing activities spurred the Ministry of Health to propose an amendment to the Food and Nutrition Safety Act of 25 August 2006. The bill provides for places where advertising of supplements is banned and addressees to whom advertising of such products cannot be directed.

In the advertising of health-related products, it is understood that the primary purpose for sometimes far-reaching restrictions is protection of the consumer's life and health, even at the expense of the consumer's right to information about the existence and properties of a given item. Particularly in the field of medical devices, Polish regulations are still more liberal than those in other EU countries. As allowed by EU regulations, they harmonise the basic rules for advertising of particular types of health-promoting products.

The legal regulations are supplemented by numerous efforts at self-regulation by the industry, in codes of ethics of such groups as Infarma, the National Pharmaceutical Manufacturers Federation, Polmed, and the National Council of Dietary Supplements and Nutritional Supplements. Admittedly, adherence to the rules in these codes is only mandatory for member companies, but in practice their importance is much greater as they the shape market practice and complement the rules contained in the law.

Particularly in the field of medical devices, Polish regulations are still more liberal than those in other EU countries.

Not every business can conduct advertising

Only a responsible entity, i.e. a business holding marketing authorisation for a given medicinal product, may advertise a medicinal product. Also, Art. 60 of the Pharmaceutical Law allows such advertising to be carried out on behalf of the responsible entity by other entities, which in practice, under a civil contract, could be for example other group companies or advertising agencies.

In turn, as of 1 January 2023, an economic operator that is a manufacturer, authorised representative, importer, distributor, or person drawing up a statement for marketing or sterilisation of systems or procedure packs is responsible for advertising of a medical device (under Art. 2(35) of the Medical Device Regulation (MDR), (EU) 2017/745). Advertising of the product may be carried out either by the economic operator itself or by an entity approved by it in writing.

Far more freedom is provided for in the Food and Nutrition Safety Act, as the current wording does not address the issue of which entities can advertise dietary supplements (nor does the proposed amendment of 23 December 2022).

Advertising addressed to the public or only to professionals

Also, Polish law narrows the circle of entities to whom advertising of healthcare products can be directed. The target group varies for different types of products. The Pharmaceutical Law provides that advertising is not allowed to be directed to the public for drugs:
– Issued by prescription only
– Containing narcotics or psychotropic substances, or
– Included in the list of drugs refunded by the national health service and authorised for dispensing without a prescription under the same name.

These medicinal products may be advertised only to professionals, i.e. persons authorised to issue prescriptions or persons trading in medicinal products.

At the beginning of 2023, provisions went into effect bringing the medical device advertising regime closer to the drug regime. Also, the Medical Devices Act provides for a ban on advertising to the public of devices intended for use by users other than laypersons, i.e. individuals with formal education in a relevant field of healthcare or medical discipline (based on the definition of “lay person” under Art. 2(38) MDR).

Use of a child’s image

Both regimes, for drugs and medical devices, are united in their ban on targeting advertising to children, regardless of the type of drug or medical device. Neither the Polish law governing trade in medicines and medical devices, nor the EU regulations relevant to these sectors, specify the children’s age. Practical guidance may be found in the Code of Ethics in Advertising, adopted by the Polish Advertising Council and the Advertising Ethics Committee, according to which “children” should be understood as persons under age 12.

Currently, there is more leeway under the standards of food law, as the Food and Nutrition Safety Act does not provide any restrictions on the addressees to whom advertising of dietary supplements can be directed. But the law may soon change, as a bill to amend this act expressly provides that it is prohibited to target advertising of dietary supplements to minors under 12 years of age, and to use children’s image or voice.

What does it mean to say that advertising is directed at children? This is determined by advertising items commonly used by children e.g. to play or learn. In rulings by the General Pharmaceutical Inspectorate, items such as colouring books, stickers, height measuring sticks, or various types of toys have been found to be banned in the advertising of medicinal products.

ADVERTISING OF HEALTH PRODUCTS

	MEDICINES	MEDICAL DEVICES	NUTRITIONAL SUPPLEMENTS
Act	Pharmaceutical Law	Medical Devices Act (Chapter 12)	Draft amendment to the Food and Nutrition Safety Act (currently no regulations on advertising)
Who can conduct advertising	Only the responsible entity or other entity commissioned by it	• Manufacturer • Authorised representative • Importer • Distributor • Person drawing up a statement for marketing or sterilisation of systems or procedure packs, and an entity approved in writing by these entities	No restrictions
Advertising to children	Ban on targeting advertising to children	Ban on targeting advertising to children	Draft ban on targeting advertising to minors under 12 years of age and ban on the use of children's image or voice
Ban on participation in advertising	• Public figures • Scientists • People with medical or pharmaceutical education	Medical professionals	Proposed ban on participation in advertising by persons practising medical professions
Warnings	Mandatory	Drafted	Drafted

ADVERTISING TARGETED TO CHILDREN

Contains items commonly used by children, e.g. for playing or learning, such as:

- Colouring books
- Stickers
- Height measuring sticks
- Various types of toys.

Will doctors vanish from commercials?

Until the end of 2022, the participation in advertising of public figures, scientists, people with medical or pharmaceutical education or suggested to have such education was banned only in the regulations governing advertising of medicinal products. Since the beginning of 2023, a similarly worded ban has also been in effect for medical devices. Art. 55 of the Medical Devices Act considers advertising of a device directed to the public unlawful if it uses images of medical practitioners or persons claiming or suggested to be members of a medical profession.

Currently, in the context of food law in Poland, such a ban does not exist, but this may soon change. The bill currently under consideration provides for a broad ban in the advertising of dietary supplements of elements that may evoke associations with the practice of healthcare professions such as doctor, pharmacist or nurse, including a ban on the use of an image or recommendation of a real or fictitious member of a medical profession.

The existing and planned provisions disallowing the use of an image of a healthcare professional are intended to counter the negative impact of marketing activities on consumer choices and to prevent dietary supplements from being mistakenly regarded as having medicinal properties. Thus the increasing tendency of Polish lawmakers to tighten restrictions on advertising in the healthcare sector may soon result in the disappearance of medical professionals from advertisements.

Obligation to post warnings

Currently, advertisers must use warnings related to the use of a given product only in the advertising of drugs, which is governed by the Regulation of the Minister of Health of 21 November 2008 on Advertising of Medicinal Products.

It should be noted that from 26 January 2023, warnings with a completely new wording must be used in advertising of medicinal products. One of the three variants indicated in the regulation may be chosen. If a new ad is released for the same medicinal product, the previous warning can no longer be used. According to the justification for the amendment, the aim of the changes is to "draw the recipient's attention to a new element of the advertising and the message contained therein." Moreover, lawmakers abandoned the existing obligation to state the counterindications in the advertising for medicinal products, because recipients are often incapable of grasping such content quickly conveyed in an ad. With this change, there is a chance that patients will more often consult the leaflet containing all the relevant information about how to use the drug and the possible counterindications.

Warnings are not required for those who advertise or promote medical devices or dietary supplements—at least for now. The issue of requiring warnings in advertising is the subject of debates on the proposed amendment to the Food and Nutrition Safety Act (in relation to dietary supplements) and the draft Regulation of the Minister of Health on Advertising of Medical Devices of 23 December 2022.

The current and planned wording of warnings used in advertising of specific regulated products from the healthcare sector is shown in the table.

WORDING OF WARNING

MEDICINAL PRODUCTS	**In audio, visual or audiovisual form:** *This is a medicine. For safety, use it according to the leaflet included in the package. Do not exceed the maximum dose. In case of doubt, consult a doctor or pharmacist.* OR *This is a medicine. For safety, use it according to the leaflet included in the package, and only when needed. In case of doubt, consult a doctor or pharmacist.* OR *This is a medicine. For safety, use it according to the leaflet included in the package. Pay attention to the counterindications. In case of doubt, consult a doctor or pharmacist.*
MEDICAL DEVICES Draft regulation (currently no regulation)	**Devices without medical applications, and accessories for medical devices:** *For safety, use according to the instructions or the label.* **Other devices, including devices for in vitro diagnostics:** *This is a medical device. For safety, use according to the instructions or the label.*
NUTRITIONAL SUPPLEMENTS Draft amendment (currently no regulation)	*A dietary supplement is a foodstuff intended to supplement a normal diet. A dietary supplement has no medicinal properties.*

What is next for influencers?

For the first time in generally applicable Polish law, the new Medical Devices Act covers advertising by influencers. However, the act does not impose specific restrictions on media personalities. Similarly, the draft Regulation of the Minister of Health on Advertising of Medical Devices does not impose additional obligations on influencers except to identify content as constituting advertising. However, influencers are to be required to provide warnings regarding medical devices they advertise.

Specific rules for influencers on advertising other types of health-promoting products do not yet exist in the generally applicable laws in Poland (except for the pharmaceutical regime, in which the advertising of medicinal products by public figures is prohibited). However, general principles and "soft law" apply. In September 2022, the president of the Office of Competition and Consumer Protection published extensive recommendations on the labelling of social media ads, which in practice have great significance for the operating model of influencers, not excluding, for example, how they advertise medical devices and dietary supplements.

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Internet of Bodies on the road to regulation

After the Internet of Things (IoT), the time has come for the Internet of Bodies (IoB). Some say we're on the way to the Internet of Everything. But for now, a few basic legal issues must be solved—even involving those omnipresent fitness trackers.

The Internet of Bodies has gained considerable interest and public acceptance due to the ease of ongoing monitoring of bodily functions, including vital signs for our health. New devices promise to diagnose and treat diseases and improve the functioning of the human body.

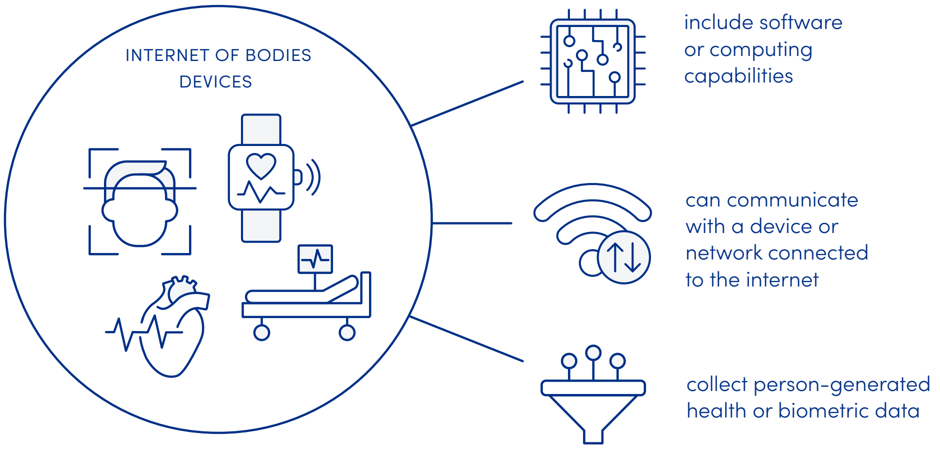
But the fashion for such devices is accompanied by an awareness that integrating the human body into the internet for the purpose of downloading, processing and exchanging data may bring negative consequences in the form of, for example, violation of users' personal integrity, invasion of privacy, inadequate data protection (especially for sensitive data), disruption of bodily functions, and even, in extreme situations, the user's death (e.g. due to interference with a pacemaker).

Therefore, there needs to be coherent and comprehensive legal regulation of digital products and services, as well as markets for such products, guaranteeing the safe operation of digital devices, and respecting and protecting the rights of users. Many acts of European law regarding these issues have already been adopted, and work on draft new regulations is underway. But it will take years to assess the comprehensiveness and effectiveness of the regulations in this area.

Internet of Bodies: What is it?

The Internet of Bodies has no legal definition. Among the various descriptive attempts, the RAND Corporation provides a clear and complete definition in its report "The Internet of Bodies: Opportunities, Risks, and Governance," according to which an IoB device is a device that:

- Includes software or computing capabilities
- Can communicate with a device or network connected to the internet
- Collects person-generated health or biometric data and/or may alter the functioning of the human body.



IoB devices can be worn on the body (wearables). This group includes the highly popular fitness-tracking electronic wristbands and smartwatches that measure basic bodily functions (pulse, blood pressure, etc), sports and other physical activities, as well as helmets and glasses that monitor, for example, work activity, but can also provide data on the user's current mental and physical state. IoB devices may include mattresses that monitor sleep or, in hospital beds, retrieve certain data on the patient's condition through body proximity technology. They may also include devices responding to the human voice or biometric authentication (such as a facial scan).

The second group of IoB devices includes invasive devices, i.e. devices inside the human body. Passive invasive devices include e.g. vascular grafts (bypasses), stents or cochlear implants. Active invasive devices are devices that communicate with an external device online, such as smart pills or cardiac pacemakers, or sensors used to stimulate the brain in neurological diseases.

Devices that look the same or similar may have different functions depending on what software they use, what network they operate on, who they send data to, and how the data is processed. A wristband may only count steps, thus measuring the physical activity of the population. But if the band measures the body's vital signs, such as pulse, blood pressure or oxygen saturation, the data it collects is health data and, as sensitive data, is subject to special protection.

The data provided by IoB devices cannot always be clearly classified. It can be hard to draw the line between sensitive and non-sensitive data. Also, data can change its nature. Data analysed and processed using artificial intelligence may change from non-sensitive to sensitive. For example, based on data tracking the user's eating habits, AI can predict the likelihood that the user will contract certain diseases.

Areas of regulation

Personal data protection

Most often, the use of IoB devices involves collection and analysis of user information. Therefore, from a regulatory point of view, personal data regulations are key. In the European Union, this means first and foremost the General Data Protection Regulation. Indeed, most often, in practice IoB operation will involve the processing of personal data within the meaning of the GDPR. And crucially, IoB devices will most often process "health data" within the meaning of the GDPR, the processing of which entails additional legal requirements.

PERSONAL DATA	any information relating to an identified or identifiable natural person ("data subject")
IDENTIFIABLE NATURAL PERSON	one who can be identified, directly or indirectly, in particular by reference to an identifier such as a name, an identification number, location data, an online identifier or to one or more factors specific to the physical, physiological, genetic, mental, economic, cultural or social identity of that natural person

Source: Art. 4 GDPR

Therefore, each aspect of IoB operations should also be evaluated for compliance of personal data processing with the requirements formulated in the GDPR. In practice, this can involve a number of legal and practical challenges, some of which we will briefly outline in the second part of the article.

Ensuring cybersecurity is key to exploiting the opportunities created by new digital technologies.

Protection of other users' rights, cybersecurity

In carrying out the tasks of the European Digital Strategy, European lawmakers have drafted a number of new regulations over the past few years and updated some currently in force. The purpose is to revamp the digital environment, its security, and the ways data can be safely and legally acquired and used, including by AI. Special regulations have also been created for certain sensitive sectors. Some of these provisions are already enacted, while other proposals are still being debated. Notably, most of the provisions enacted or proposed in this area are in the form of a regulation, rather than a directive. This ensures the harmonisation of regulations relating to digital technologies across the EU, which is also relevant to the IoB.

Among these regulations, several groups can be highlighted. For the Internet of Bodies, the fundamental provisions include:

– Data Governance Act (Regulation (EU) 2022/868 on European data governance)
– Data Act (Proposal for a Regulation of the European Parliament and of the Council on harmonised rules on fair access to and use of data)
– European Health Data Space (proposed regulation)
– Medical Device Regulation (2017/745)
– Regulation (EU) 2019/1020 on market surveillance and compliance of products.

The second group of regulations under preparation includes the Artificial Intelligence Act (Proposal for a Regulation of the European Parliament and of the Council laying down harmonised rules on artificial intelligence) and the proposed AI Liability Directive. Work on them is ongoing. Without regulating these issues, the IoB security system will not be closed.

Significant rules for digital services and digital markets are introduced by Regulation 2022/2065 and Regulation 2022/1925. Among other things, they are intended to provide a secure digital space in which the basic rights of users, including users of IoB devices, are protected.

The protection of rights of IoB device users will also be ensured, once transposed into national law, by the Digital Content Directive (2019/770), and by the proposal for a revised Product Liability Directive, with AI systems and goods based on them being deemed to be products.

Ensuring cybersecurity is key to exploiting the opportunities created by new digital technologies. The Cybersecurity Act (Regulation 2019/881) establishes certification requirements for networks and information systems, as well as related services and processes. Two directives adopted at the end of 2022 govern, respectively, measures for a high common level of cybersecurity (NIS2 Directive, 2022/2555) and the resilience of critical entities (2022/2557), which include some entities from the healthcare sector. Work is also underway on a European Cyber Resilience Act, governing security requirements for products with digital elements.

REGULATIONS RELEVANT TO DIGITAL TECHNOLOGIES

Key for the Internet of Bodies:

- Data Governance Act (Regulation (EU) 2022/868)
- Data Act (draft EU regulation)
- European Health Data Space (proposed EU regulation)
- Medical Device Regulation ((EU) 2017/745)
- Regulation on market surveillance and compliance of products ((EU) 2019/1020)

Additional:

- Artificial Intelligence Act (proposed EU regulation)
- AI Liability Directive (proposal)
- Digital Services Act (Regulation (EU) 2022/2065)
- Digital Markets Act (Regulation (EU) 2022/1925)

Protection of the rights of users of IoB devices:

- Digital Content Directive (2019/770) (after transposition into national law)
- Product Liability Directive (proposal)

Ensuring cybersecurity:

- Cybersecurity Act (Regulation (EU) 2019/881)—certification requirements for networks, information systems, and related services and processes
- NIS2 Directive (2022/2555)—measures for a high common level of cybersecurity
- Directive (EU) 2022/2557 on the resilience of critical entities

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GDPR: Legal and practical challenges

The compliance principle of data processing

Under the GDPR, for processing of personal data to be considered permissible, an entity processing personal data for its own purposes must have one of the grounds for processing personal data indicated in the GDPR. The permissible grounds for processing health data are indicated in Art. 9(2) GDPR. Examining this provision in terms of the basis for processing health data best suited to the operation of the IoB generates a number of questions and reveals a number of potential associated challenges.

For the IoB in standard circumstances, the basis for processing health data could be:

1. Explicit consent of the data subject to the processing of such personal data for one or more specified purposes
2. Necessity of the processing for purposes of preventive or occupational medicine, for assessment of the working capacity of the employee, medical diagnosis, provision of health or social care, treatment or management of health or social care systems and services on the basis of EU law or member state law or pursuant to contract with a health professional and subject to the conditions and safeguards referred to in Art. 9(3) GDPR
3. Necessity of the processing for reasons of public interest in the field of public health, such as protection against serious cross-border health threats or ensuring high standards of quality and safety of healthcare and medicinal products or medical devices, on the basis of EU law or member state law that provides for appropriate specific measures to protect the rights and freedoms of data subjects, in particular professional secrecy.

The grounds indicated in points 2 and 3 may find application if the IoB devices are used in the context of, for example, medical diagnosis or for reasons linked to public health, and the data processing carried out by the IoB is necessary to achieve the purposes to which the indicated grounds for processing apply. In practice, these grounds will apply only in specific cases when the IoB tools will be used by medical personnel as part of broadly defined healthcare conducted under EU or local regulations (meaning that IoB devices intended for self-use by consumers will not process data under these grounds).

Assuming that the grounds indicated in points 2 and 3 are adequate for specific IoB devices, additional doubts may arise as to the extent to which the processing carried out by the IoB will be carried out subject to the safeguards and with the application of measures referred to in the cited provisions.

In general, the indicated bases assume that the processing of health data will be carried out by properly trained medical personnel, who are obliged to maintain professional secrecy. However, IoB devices can operate (and often operate in practice) based on external computing power (e.g. in the cloud), which means that the data they process could be accessed by persons not covered by professional secrecy, which in turn could preclude the possibility of basing health data processing on the indicated grounds. Therefore, in practice, even in the case of IoB devices used in the broader healthcare field, the technical aspects of IoB operation would need to be analysed to eliminate these risks.

In the case of IoB devices intended for independent non-medical use, in principle the only basis for processing health data could be the consent of the data subject. However, relying on consent raises a number of challenges. Indeed, the GDPR indicates that for consent to process health data to be valid, it must be express, voluntary, specific and consciously given. In particular, this means that the consent should be worded in such a way that it does not cover several purposes of processing and that the data subject, when giving consent, understands what data processing he or she is accepting. Additionally, the validity of consent is dependent on whether the person is actually free to make a choice to give consent (i.e. among other things, whether they feel pressured to consent, or failure to consent will result in negative consequences for them). Given the nature of the IoB's operations, the formulation of appropriate consent may be problematic. Moreover, the consent to processing of health data must be "explicit." Therefore, it must be granted in a manner not raising doubts about the content, the person consenting, the circumstances, and the fact of granting consent. The most common way to obtain this type of consent is through a written statement from the data subject. In the case of IoB, obtaining "explicit consent" from users to process health data can be made more difficult.

Additionally, IoB devices often use the collected health data not only for operation of a particular device, but also for broader development of the IoB device or solution, for example development of software for data analysis or improving the functionality

For consent to process health data to be valid, it must be express, voluntary, specific and consciously given.

The large data sets collected by the IoB may be used secondarily for the purposes of development of other IoB solutions or similar products.

or efficiency of the IoB. It is difficult to find a basis in Art. 9(2) GDPR for processing health data for this purpose. Therefore it seems that to use data for IoB development, to be on the safe side the data would have to be fully and irreversibly anonymised beforehand.

The large data sets collected by the IoB may be used secondarily for the purposes of development of other IoB solutions or similar products (e.g. using AI) or even for scientific purposes. In the case of processing for scientific purposes, the basis for the processing could potentially be Art. 9(2)(j) GDPR, according to which the processing of health data is permitted if it is necessary for the purposes of scientific research under the law of the European Union or a member state, and the law:

– Is proportionate to the aim pursued
– Respects the essence of the right to data protection, and
– Provides for suitable and specific measures to safeguard the fundamental rights and the interests of the data subject.

What may prove problematic is the extent to which issues of scientific research using data obtained from the IoB are regulated by EU or member state law in such a way that the processing of data from the IoB can be covered by Art. 9(2)(j) GDPR. The extent to which the processing of non-anonymised personal data is actually necessary for purposes of scientific research may also prove problematic, as it seems that, in principle, processing of anonymised data may be sufficient to achieve the aims of the research. Anonymisation of IoB-acquired data could also enable secondary use of the data for other commercial purposes (not involving scientific research), for example, to feed AI algorithms.

A separate issue is the legal nature of databases collected by the IoB and the right to use such databases, but this issue goes beyond the sphere of data protection law and intersects with regulations governing databases and potentially intellectual property law.

Transparency of processing

The GDPR imposes on processors of personal data the duty to transparently inform data subjects about the processing of their data at the time of collection. The GDPR provides that the information must be presented concisely, clearly, in an understandable and easily accessible form, in clear and simple language. At the same time, Art. 13 GDPR specifies the scope of information to be provided to the data subject. These obligations also apply to IoB devices.

If an IoB device processes a user's personal data, the user should be provided with relevant processing information at the start of data collection (e.g. on startup of the device). With that said, the nature of operation of IoB devices (especially in the case of more complex products) can make it very difficult to present comprehensive, transparent and concise information to the extent required by the GDPR (especially if the device has no display or is very small). Additionally, it must be taken into account that, as a rule, the information should be presented in a language familiar to the user of the IoB device. Thus, if the IoB device is intended for users throughout the EU, the information about processing of personal data should be prepared in all official languages of the member states.

Data protection impact assessment

In general, a data protection impact assessment (DPIA) of planned processing operations is a type of analysis where the data controller should, among other things, comprehensively describe:

– The technical method of processing data
– Risks to data subjects associated with the processing of their data
– Measures planned to be applied to address the risks
– Measures the controller will apply to ensure compliance of the data processing with the GDPR.

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DATA PROTECTION IMPACT ASSESSMENT

Where a type of processing in particular using new technologies, and taking into account the nature, scope, context and purposes of the processing, is likely to result in a high risk to the rights and freedoms of natural persons, the controller shall, prior to the processing, carry out an assessment of the impact of the envisaged processing operations on the protection of personal data. A single assessment may address a set of similar processing operations that present similar high risks.

Source: Art. 35(1) GDPR

Often, IoB devices may require a mandatory DPIA due to the specificity of their operation and because they process health-related data. Conducting a DPIA may be a practical challenge and require a multidisciplinary team of specialists. However, it would be a useful approach not to treat this as an onerous obligation, but as an opportunity for a holistic analysis of the data processes carried out by IoB devices for the purpose of minimising the risks of non-compliance with the GDPR.

Exercise of data subjects' rights

The GDPR grants individuals whose personal data is processed a number of rights related to the processing. Under the GDPR, the controller of the data must also ensure that data subjects have an actual opportunity to exercise their rights. In practice, this can be quite a challenge. For example, pursuant to the GDPR, data subjects may request:

1. **Provision of a copy of the data related to them** and, in some situations, also transmission in electronic form to a designated recipient. This means that the data must be easily extractable and formatted in such a way that it can be securely transmitted and read using generally available means (and not by the device's own proprietary software).
2. **Deletion of data relating to them**. This means that there must be a technical possibility of irreversibly deleting the data generated by the IoB device from the controller's databases, or anonymising the data. This can be problematic when the data is used to "train" the IoB device, or when the structure of the databases is such that removing selected data will reduce the utility of the entire database.

It should be apparent that the operation of IoB devices is complex and touches on a range of legal areas. The regulations will have to keep pace with the progress of further spread of the Internet of Bodies and changes in the IoB devices used.

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Is labour law ready for the metaverse?

Since 28 October 2021, when Facebook CEO Mark Zuckerberg announced that he was renaming his tech empire Meta and planned to create a metaverse, countless articles have been written about this concept. But most of them focus on the key issues of data protection and intellectual property rights. Relatively little space is devoted to considering how the spread of the metaverse will affect the work environment.

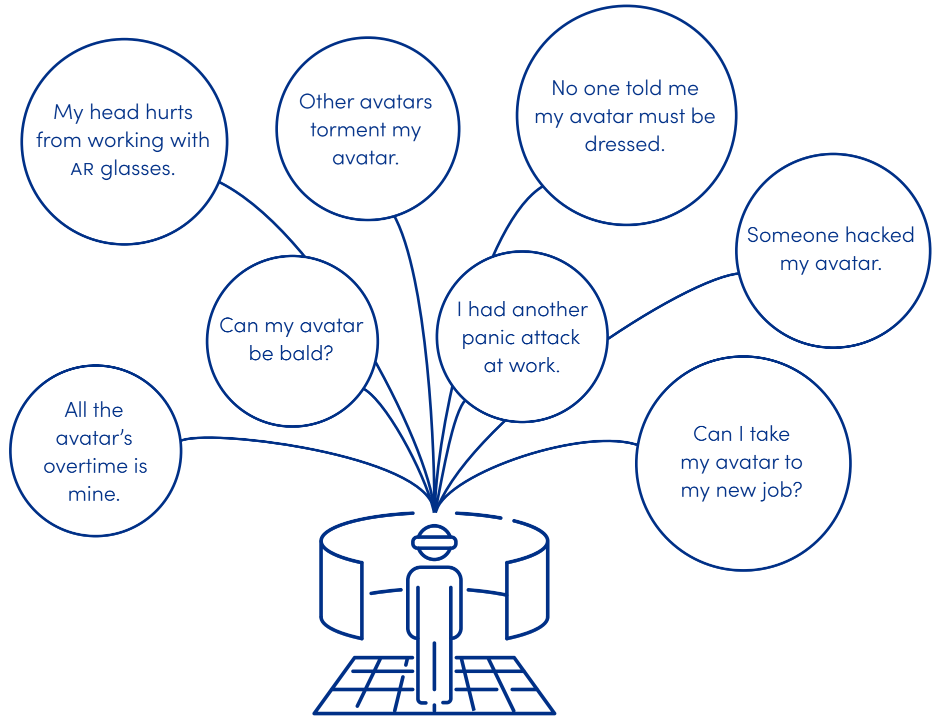
A song of the future or a new tomorrow for employees?

The concept of the metaverse first appeared in Neal Stephenson's 1992 cyberpunk novel *Snow Crash*. Since Zuckerberg's memorable presentation, this term has virtually never left the front pages of paper and online publications. But there is still no consensus on which form of metaverse this will involve: a parallel digital world, where users have the impression of being almost fully immersed in a virtual space, at the same time having the possibility of interaction with the surroundings (the association with *The Matrix* is most relevant here), or another enhanced version of augmented reality, where a virtual layer is imposed on the real world, allowing the user's actions in the physical world to be linked to selected elements and functionalities of the virtual world (here, in turn, cinema suggests a vision from Steven Spielberg's *Minority Report*, in which the main character "juggles" data, images and documents).

Experts estimate conservatively that it could take up to 10 years (if it happens at all) for Zuckerberg's vision to become "reality," depending on the degree of complexity of the metaverse and, most importantly, the pace of development and spread of 5G technology, WiFi 6 and edge computing, as well as the successors to these technologies, which are essential for the proper and stable operation of the metaverse. For the time being, technology does not allow the transmission of such a huge amount of data without delays and loss of quality of the transmitted images and sounds. The use of the metaverse at work may also be limited due to the price of the equipment (primarily AR glasses, VR gloves, etc) and (at least currently) the discomfort of using this equipment for extended periods (anyone who tries to replicate the aforementioned motions by the *Minority Report* protagonist for more than a few minutes or sits in AR glasses for longer will quickly understand where the problem lies).

None of this seems to bother metaverse enthusiasts. For example, several renowned law firms from Europe and the United States have already opened offices in the metaverse.

But even if the metaverse is still a song of the near or distant future, it is vital to remember that labour law already lags behind the development of digital technologies (the best example is the regulation of remote work, which we write about on p. 6), and changes in law are not enacted overnight (or, assuredly, should not be). Therefore, drawing on their experience with existing technologies, it would be worthwhile for lawmakers and labour market participants to start a practical discussion now on how to prepare for the changes coming in the next decade, while at the same time maintaining the delicate balance between supporting the growth of innovation and protecting the safety and rights of users in the workplace.



difficulty working in the metaverse

The challenges of the virtual workplace

It can be expected that persons using the metaverse as a working tool or even a work environment will first face the same challenges as users of existing digital solutions, including social media. But undoubtedly the metaverse will also generate unprecedented new issues.

One such challenge is the use of avatars by employees while performing their job duties. As in the case of social media accounts, it seems that employers will not be able to force employees to open accounts and create an individually assigned avatar for work purposes, in particular an avatar that faithfully reflects the employee's actual appearance—skin colour, gender (biological or cultural), age, disability, or even elements enabling identification of the user's nationality, ethnicity or religion. This would require the employee to provide the platform operator with personal data, including potentially sensitive data and the employee's image.

On the other hand, under Polish labour law, in our view there is no obstacle to making a candidate's employment conditional on possessing a metaverse account (avatar), as long as such a condition of employment is closely related to the nature of the job offered (e.g. in the communications or online marketing department). But the risk that the data protection authority would object to this practice cannot be completely ruled out.

The scope of labour law issues relating to work avatars may depend, among other things, on whether the avatar is assigned to a specific employee/user and has his or her characteristics, or the avatar is assigned to the employer and merely operated by an authorised employee, without necessarily reflecting the employee's individual appearance (e.g. an avatar in the form of a "mascot" or stylised company logo).

This distinction between an avatar as the employee's "digital twin" in the metaverse and an avatar as a working tool may be relevant to the legal evaluation of such situations as:

– **Discrimination against an employee based on the avatar's characteristics.** An even more intriguing problem is whether there could be said to be discrimination against an employee based on characteristics (e.g. gender or skin colour) that the avatar possesses, but the real user does not.

– **Employee responsibility for the avatar's appearance or behaviour, e.g. compliance with the company's dress code.** We can imagine a situation where an avatar appears at a virtual meeting with a client of the company dressed inappropriately for the situation (or even naked) or displaying features (such as a T-shirt or tattoos) with offensive or racist content. Businesses are already putting in place internal policies, sometimes very elaborate and detailed, governing the use of digital tools as part of the job. It can be expected that the new form of employees' virtual activity will require supplementing existing policies or even enacting all-new "meta-policies." Another situation would be where the avatar is stolen or hacked, and how this would be proved in the context of holding employees accountable for misuse of their avatars. Bearing in mind how closely the algorithms and databases of digital platforms are guarded today as trade secrets, in the event of a dispute with an employee, obtaining such data for evidence purposes could be difficult or impossible in practice.
– **Permissibility of monitoring employee activity in the metaverse,** including for the purpose of accounting for employee time. If a company avatar is used by several employees, it could be a problem to determine who was present in the metaverse and for how long.
– **Use of a company avatar after an employee ceases working for the employer**, including in the context of whether the avatar must be "returned" to the employer or deactivated upon termination of employment, or whether employees can continue using avatars they created or operated at one job, when working for a new employer (particularly a competitor of the former employer).

Employee safety in the virtual universe

The entry into the metaverse and the professional activity of employees in this medium will also have to be reflected in the obligation to provide employees with safe and healthy working conditions. One of the first issues that arises in this context is effective protection of employees from cyberbullying and other forms of violence in the virtual world, whether from co-workers or from people outside the organisation. Research to date shows that cyberbullying in a digital workplace can occur with greater intensity (for a number of reasons, such as the illusion of anonymity) than "traditional" mobbing, and that preventing this form of violence in the virtual work environment is much more difficult. And it seems that many organisations are already failing to deal with this problem.

Pursuant to Art. 207 §2 of the Polish Labour Code, every employer is obliged to protect the life and health of employees with appropriate use of scientific and technological achievements, including responding to occupational health and safety needs, adopting protective measures taking into account the changing conditions for performance of work, and implementing a consistent policy for preventing accidents at work and occupational diseases, taking into account technical issues, working conditions, and the impact of working environment factors. Thus employers' health and safety rules will have to be revised to take into consideration the new technologies linked with a presence in the metaverse, such as the use of AR glasses and their impact on employees' physical and mental health. Among other things, persons testing prolonged use of AR glasses reported dizziness and headaches, nausea, visual fatigue, but also fatigue caused by unusual and excessive stimuli (in the pandemic, employees got a dose of this in the form of "Zoom fatigue"), mood deterioration, or even panic attacks. Therefore, it may quickly turn out that these risks to employee health need to be reflected e.g. in occupational health and safety training, referrals for specialised (and thus quite expensive) medical examinations, or occupational risk assessments.

Is there anything to look forward to?

When announcing his project, Mark Zuckerberg enthusiastically presented the advantages of moving work to the metaverse. Among the benefits for employers and employees, he cited:
– Easier relationship-building and smoother cooperation between employees working remotely
– Faster onboarding of new hires
– Higher quality of remote training
– Lower demand for office space.

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Cyberbullying in a digital workplace can occur with greater intensity (for a number of reasons, such as the illusion of anonymity) than "traditional" mobbing.

To this list of advantages we might add further expansion of the talent pool from which employers can draw, e.g. by including the possibility to hire employees from every corner of the globe and activating people previously barred from "analogue" work (e.g. caregivers or people with disabilities).

The metaverse will rather be an additional work tool or a solution supporting employee onboarding and training, and not a full new work environment in which employees spend most of the working day.

On the other hand, in the employment context, sceptics of the metaverse point out such risks as:

- Further stratification of the employment market by the criterion of the ability to participate in the metaverse (e.g. for health reasons, not every worker will be able to use AR glasses, not to mention other items of equipment for work in the metaverse)
- Replacement of real employees by virtual tools (advanced chatbots, virtual assistants, etc)
- Hiring from countries with weak protection of workers
- Less opportunity for remote workers to unionise or strike.

So far employers seem to be taking a cautious approach to the use of the metaverse at work. From studies conducted among businesses, it can be concluded that the metaverse will rather be an additional work tool or a solution supporting employee onboarding and training, and not a full new work environment in which employees spend most of the working day. The coming decade will show what potential, but also risks, the metaverse brings to the employment market.

We have barely scratched the surface of the aspects of labour law that may be impacted by the wider use of the possibilities offered by the metaverse. But we hope that our article helps further the discussion on changes in labour law that may be necessary for the law to keep up with the rapidly evolving virtual world.

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Limitations on financial claims over state aid

When financial claims arising out of irregularities in the granting of state aid become time-barred is an issue as complex as the value of the potential irregularities is great. Knowledge of the mechanisms for determining the limitations period with respect to irregularities may protect against liability, including the duty to repay state aid obtained in the past.

Generally, when we say that something is time-barred, it means that the perpetrator can no longer be punished a certain time after commission of a prohibited act (limitation on punishability) or a punishment against the person can no longer be executed (limitation on enforcement of a punishment). This is hugely important for anyone committing such acts, including under the law of state aid, where this applies in particular when there have been irregularities in granting or spending state aid.

The law of state aid employs various limitation periods on claims, which can be distinguished based on how the public body acts in the given matter. Simply determining the limitation period on claims arising out of state aid is not enough to precisely define the date when the claim becomes time-barred, because it also depends on the date from which the limitation period should be counted.

Entity taking action

If the European Commission is acting in a given matter, the limitation period is 10 years, which is expressly provided in Art. 17(1) of Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union ("The powers of the Commission to recover aid shall be subject to a limitation period of 10 years").

As the Court of Justice of the European Union has held in two cases (C-387/17, *Fallimento Traghetti del Mediterraneo SpA*, and C-349/17, *Eesti Pagar*), for the sake of legal certainty, the 10-year limitation period provided in Regulation 2015/1589 cannot be applied in national proceedings, but applies only to the Commission.

The rules governing limitations on irregularities affecting the financial interests of the European Union are established in Art. 3 of Council Regulation (EC, Euratom) No 2988/95 of 18 December 1995 on the protection of the European Communities financial interests, introducing general rules for uniform oversight, recovery of EU funds spent as a result of irregularities, and imposition of related penalties. Under Art. 1 of that regulation, it extends to "irregularities with regard to Community [EU] law," defined as "any infringement of a provision of Community law resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities or budgets managed by them, either by reducing or losing revenue accruing from own resources collected directly on behalf of the Communities, or by an unjustified item of expenditure."

Based on the case law from the Court of Justice, the limitations provisions of Art. 3 of Regulation 2988/1995 exert direct effect, and thus can be the immediate legal basis for rulings by national bodies in proceedings conducted by them.

Limitation period on irregularities—main period, shorter and longer periods

The main limitation period on irregularities is defined in the first paragraph of Art. 3(1) of Regulation 2988/1995 as four years from the time the irregularity was committed.

EU sectoral rules (such as rules under the Cohesion Policy) may (but need not) provide for a shorter period, but it may not be less than three years.

The law of state aid employs various limitation periods on claims, which can be distinguished based on how the public body acts in the given matter.

Meanwhile, under Art. 3(3) of the same regulation, member states may apply limitation periods longer than the four-year period provided for in that article. However, when setting limitation periods, the member states must observe the general principles of EU law, particularly the principle of proportionality.

Polish regulations setting limitation periods on irregularities

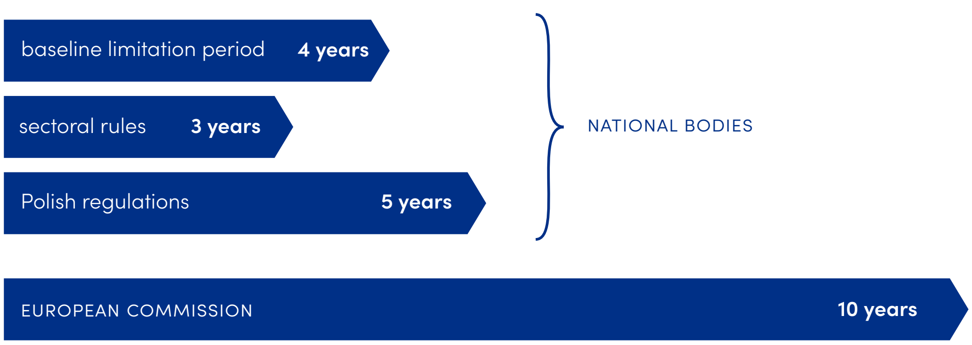
Under Art. 66a in connection with Art. 60(6) of the Public Finance Act, the limitation period on the obligation to repay funds intended for implementation of programmes financed with the involvement of European funds and other receivables related to execution of projects financed with the involvement of such funds, as well as interest on such funds or receivables, is five years. In light of the position adopted by the Court of Justice for example in C-584/15, *Glencore Céréales France*, upholding the proportionality of a five-year limitation period, it should be recognised that the five-year limitation period for irregularities established by the Polish regulations is also consistent with the principle of proportionality.

Duration and recurrence of irregularities

The limitation period on irregularities runs from the date of commission of the act. The Court of Justice takes the view that occurrence of an irregularity requires fulfilment of two conditions:
– An act or omission constituting an infringement of EU law
– Actual or potential injury to the EU budget resulting from the infringement.

Consequently, the limitation period on irregularities begins to run from the time of the act or omission constituting an infringement of EU law, or occurrence

LIMITATION PERIODS ON IRREGULARITIES IN STATE AID



of a detriment to the EU budget, but the decisive point is always the occurrence of the last of these events. And according to the case law of the Court of Justice, for determination of the time when the limitation period on irregularities begins to run, it is irrelevant when the irregularity was discovered, or that it was disclosed after occurrence of the detriment to EU funds. Thus, even more, commencement of running of the limitation period should not be tied to the date of issuance of the final administrative decision ordering return of the aid. This position is also shared by the Polish administrative courts (Supreme Administrative Court judgment of 18 May 2017, case no. II GSK 4503/16).

Commencement of running of the limitation period depends on the type of irregularity. The limitation period on a one-off irregularity begins to run upon commission of the act meeting the definition of the offence. However, in the case of continuous or recurring irregularities, the limitation period runs from the date when the irregularity ceased (C-279/05, *Vonk Dairy Products*). In the case of multiannual programmes (i.e. those lasting for at least two years), the limitation period on irregularities runs from the final completion of the programme, even if the multiannual programme lasts longer than four years (C-436/15, *Alytaus regiono atliekų tvarkymo centras*).

Limitation of interest

Under Art. 4(1) of Regulation 2988/1995, "As a general rule, any irregularity shall involve withdrawal of the wrongly obtained advantage." However, under Art. 4(2), recovery "shall be limited to the withdrawal of the advantage obtained plus, where so provided for, interest which may be determined on a flat-rate basis."

Art. 3 of the regulation also applies to the limitation on interest, but does not apply if interest is sought exclusively based on national law, not EU law.

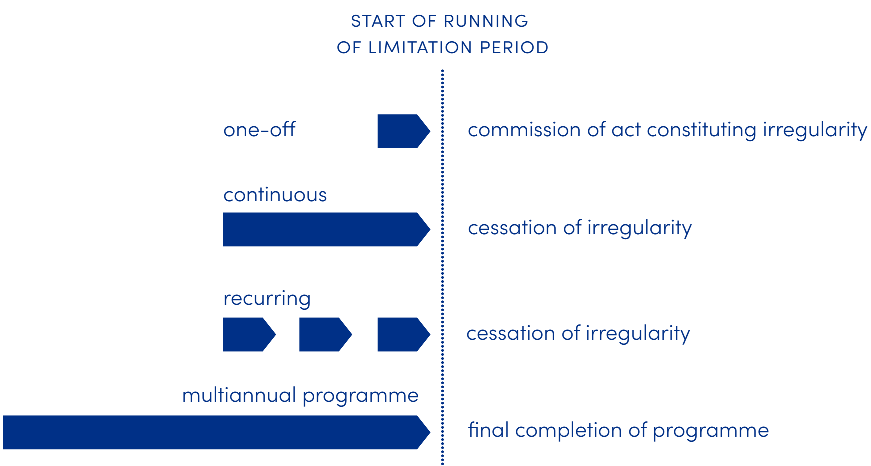
Interruption of the limitation period on irregularities

The limitation period on irregularities is interrupted by any act by the competent authority involving an investigation or proceedings concerning the irregularity, of which the relevant person is notified. After each interruption, the limitation period begins to run anew.

The competent authority is the authority entitled to conduct an investigation or proceedings concerning the irregularity, which need not be the body authorised to award the subsidy or recover amounts spent as a result of an irregularity. In turn, the relevant person who is to be notified is the entity suspected of committing the irregularity that is the subject of the investigation or proceeding. In the case of a legal person, an individual whose behaviour may be attributed to the legal person under national law should be notified. But to effectively interrupt the running of the limitation period on the irregularity, the

COMMENCEMENT OF RUNNING OF LIMITATION PERIOD ON IRREGULARITIES IN STATE AID — COMMISSION OF THE IRREGULARITY

TYPES OF IRREGULARITIES IN STATE AID AND START OF RUNNING OF THE LIMITATION PERIOD



Limitation shall become effective at the latest on the day on which a period equal to twice the limitation period expires without the competent authority having imposed a penalty.

notification must identify with sufficient precision the transactions with respect to which the commission of irregularities is suspected (C-52/14, *Pfeifer & Langen*). It thus cannot arise out of notification of routine oversight activities by national authorities unconnected with the suspected irregularities (C-278/02, *Handlbauer*).

Firm deadline for limitation of claims over irregularities

Under the fourth paragraph of Art. 3(1) of Regulation 2988/1995, "limitation shall become effective at the latest on the day on which a period equal to twice the limitation period expires without the competent authority having imposed a penalty, except where the administrative procedure has been suspended in accordance with Article 6(1)."

This period is applied:

– In proceedings aimed at imposing administrative penalties for commission of irregularities
– In proceedings aimed at recovering amounts spent as a result of irregularities (C-383/14, *Sodiaal International*)
– For purposes of seeking interest on returned amounts received as a result of irregularities (C-584/15, *Glencore Céréales France*).

… and again the Commission

As a rule, national regulations apply with respect to recovery of unlawfully awarded aid at the national authorities' own initiative. But this does not detract from the possibility of subsequent recovery of the aid in implementation of a decision to that effect by the European Commission. If the Commission has information in its possession on the alleged unlawfulness of the aid, whatever the source of the information, after the national limitation periods have expired, the Commission retains the right to examine the aid within the period of ten years referred to in Art. 17(1) of Regulation 2015/1589 (Art. 15 of Regulation 659/1999, see C-349/17, *Eesti Pagar*).

Summary

Evidently, parties sometimes prematurely breathe a sigh of relief in the belief that claims over irregularities in state aid have become time-barred. The European Union looks after its financial interests, which on one hand benefits all of us, but on the other hand can be troublesome for businesses which have improperly received or disbursed state aid.

EWA KRUSZKO
attorney-at-law,
Restructuring & Bankruptcy practice

The Second Chance Directive: New tools for distressed businesses

The satisfaction test will give creditors a basis for an informed vote on an arrangement. The rules for protection from enforcement will be the same in all preventive restructuring proceedings, and secured claims will also be covered by an arrangement. These changes are likely to happen in 2024.

A bill to amend the Restructuring Law of 15 May 2015 and the Bankruptcy Law of 28 February 2003 was published on the website of Poland's Government Legislation Centre on 4 July 2022. The purpose of the amendment is to implement into the Polish legal system Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132.

Directive 2019/1023 is commonly referred to as the "Second Chance Directive," as one of its key elements is to ensure that insolvent businesses have access to at least one type of proceeding that can lead to complete debt relief.

According to the aims of Directive 2019/1023, the preventive restructuring framework should first and foremost enable debtors to restructure effectively at an early stage and avoid insolvency, thereby reducing unnecessary liquidation of viable businesses.

Directive 2019/1023 is already largely reflected in the Bankruptcy Law and the Restructuring Law in Poland. However, full implementation of the directive will bring several important changes, especially from the point of view of creditors, including:

– Temporary limitation of anti-enforcement protection
– A new mechanism for approving an arrangement over the objection of a class of creditors
– Mandatory inclusion of secured claims in the arrangement by operation of law.

> **The ban on conducting enforcement in restructuring proceedings would extend to all of the debtor's assets.**

Remedial proceedings outside preventive restructuring

The amendment provides for a clear distinction between preventive restructuring proceedings (i.e. proceedings for approval of an arrangement (*postępowanie o zatwierdzenie układu*), accelerated arrangement proceedings (*przyspieszone postępowanie układowe*), and arrangement proceedings (*postępowanie układowe*)) on the one hand, and remedial proceedings (*postępowanie sanacyjne*) on the other. Remedial proceedings, which are proceedings of a special nature allowing for deep restructuring of a business, remain outside the scope of application of Directive 2019/1023. Henceforth, it will be possible to conduct remedial proceedings only against an insolvent debtor. Meanwhile, preventive restructuring proceedings will remain proceedings intended either for debtors threatened with insolvency or for insolvent debtors.

The satisfaction test

One of the most significant changes in the proposed amendment is introduction of the institution of the "satisfaction test."

The supervisor or administrator will be required to draw up the satisfaction test, which will include a valuation of the debtor's business in three options, that is in the case of:

– Implementation of the restructuring plan
– Sale of the debtor's business as a whole in bankruptcy proceedings
– Sale of individual components of the debtor's business in bankruptcy proceedings.

The satisfaction test is also to include information on the anticipated degree of satisfaction of the claims of the creditors participating in the arrangement in possible bankruptcy proceedings. The supervisor or administrator will also provide an assessment of whether a higher degree of satisfaction of claims covered by the arrangement can be obtained under the arrangement or in the event of bankruptcy.

This will provide creditors with adequate material allowing them to make an informed decision on how to vote on the arrangement. On the basis of this document, a creditor will be able to assess whether it will be more advantageous to conclude an arrangement in the course of restructuring proceedings or to obtain satisfaction in possible bankruptcy proceedings.

Conducting such a simulation is also important from the point of view of the proposed changes to the grounds for refusal to approve the arrangement. Indeed, under the amended Art. 165(2) of the Restructuring Law, the court would have to refuse to approve the arrangement if any creditor who voted against the arrangement and raised objections would be worse off as a result of the arrangement than if bankruptcy proceedings were carried out or if the restructuring proceedings were terminated without approving the arrangement. Thus, at the same time, the result of the satisfaction test will serve as a benchmark for evaluating implementation of this basis for refusing to approve the arrangement.

Temporary limitation of protection from enforcement

The bill provides for unification of the rules governing protection from enforcement during restructuring and introduces a temporary limitation on such protection.

In the current wording, the Restructuring Law differentiates in the scope of protection from enforcement depending on the type of proceeding chosen, and this protection can consist of limiting the permissibility of directing enforcement only against collateral, or a total ban on conducting enforcement.

According to the proposed new rules, the ban on conducting enforcement in restructuring proceedings would extend to all of the debtor's assets, which also applies to enforcement against collateral held by secured creditors.

The proposed temporary nature of such protection will be an important new feature. This solution arises out of Art. 6(6) of Directive 2019/1023, which provides that the initial period of suspension of individual enforcement measures is limited to a maximum of four months. The member states may extend this period to up to 12 months.

Today, the protection from enforcement in restructuring proceedings basically lasts from the moment of opening of the proceedings until their final and binding conclusion or discontinuance. Currently, the time limitation on enforcement applies only in proceedings for approval of an arrangement. After the proposed amendments enter into force, such a solution will cover all types of restructuring proceedings.

The anti-enforcement protection will last for four months. The new rules provide for the possibility of extending this for a further period, not exceeding, together with the period of the original suspension, 12 months (if circumstances indicate that entering into an arrangement is likely). Additionally, in remedial proceedings, the initial period of protection from enforcement will be 12 months, with the possibility of extension by the judge-commissioner (in this case, without an upper limit).

As a rule, the protection from enforcement will begin on the day the restructuring proceedings are opened. However, at the request of the debtor, this protection may begin as early as the date of announcement of the order of entry in the registry of the restructuring application filed by the debtor (and will then last for four months from the date of the announcement). The aim of this solution is to allow the debtor to be protected from enforcement from the first moment that the information on the debtor's filing of the application to open restructuring proceedings is publicly announced, as from that moment the risk of creditors taking or intensifying enforcement measures increases. At the same time, filing of such an application by a debtor will have the effect of limiting its right to administer its assets to the ordinary course of business during the period between the date of the announcement and the date on which restructuring proceedings are opened, which is justified by the need to protect the interests of creditors.

The bill also rightly provides for suspension by operation of law of individual enforcement proceedings from the date of approving the arrangement until the date of completion or final discontinuance of the restructuring proceedings by the court. Indeed, the absence of such protection could nullify the effects of the concluded arrangement.

Changes regarding secured creditors

Following Directive 2019/1023, the bill also introduces mandatory inclusion of secured claims in the arrangement, by virtue of law, regardless of the content of the arrangement proposals.

As the catalogue of claims that member states may exclude from the scope of the preventive restructuring framework is exhaustively set forth in Art. 1(5) of Directive 2019/1023, any other categories of claims must be unconditionally covered by the arrangement. Therefore, it was necessary to remove secured claims from the catalogue of claims optionally subject to the arrangement.

Instead, the Polish parliament has provided a number of guarantees for secured creditors to ensure proper protection of the interests of this category of creditors.

First, creditors of this type cannot be satisfied at a lower rate in the arrangement than in a possible bankruptcy proceeding, unless they agree to such less favourable satisfaction terms.

Second, the arrangement proposals for such creditors should not provide for any other method of satisfaction than that provided for in the agreement (unless the creditor agrees to a different method). Thus, for example, it will not be possible to formulate arrangement proposals involving the conversion of a secured creditor's claims into shares in the debtor, without the consent of such creditor.

Liquidation arrangement under new rules

Another new feature will be the possibility of entering into a liquidation arrangement providing for the sale of the debtor's assets with enforcement effect (i.e. without encumbrances such as mortgages and pledges).

Under current law, a sale made in implementation of an arrangement providing for satisfaction of creditors via the liquidation of the debtor's assets does not cause the effects of an enforcement sale. In certain situations, only remedial proceedings give the administrator the opportunity to sell the debtor's assets unencumbered.

However, the liquidation of an encumbered asset (e.g. under a mortgage, ordinary pledge or registered pledge) in this manner will be possible only with the consent of the secured creditor.

PROTECTION AGAINST ENFORCEMENT

Before amendment	Proposed amendment
• Scope of protection against enforcement depends on the type of proceeding • Protection against enforcement in restructuring proceedings basically runs from opening of the proceedings until legally final completion or discontinuance	• Uniform rules for protection against enforcement in all preventive restructuring proceedings • Ban on enforcement will extend to all of the debtor's assets and will also cover secured creditors • Introduction of temporary protection against enforcement (initial period of protection is to be four months)

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Further, the protection of secured creditors is to be ensured by judicial review of the preparation and implementation of a separate plan for distribution of proceeds obtained from the liquidation of the encumbered property, which is to be based on the principles provided for in the Bankruptcy Law.

LIQUIDATION ARRANGEMENT

Before amendment	Proposed amendment
• Arrangement may provide for liquidation of the debtor's assets, BUT • Sale of the debtor's assets in implementation of the arrangement does not have the effect of an enforcement sale	• New tool for creditors—possible liquidation arrangement with the effect of an enforcement sale • Necessary consent of secured creditor to liquidate collateral • Separate plan to be drawn up for distribution of proceeds from liquidation of collateral • Can offer an attractive alternative to sale of the debtor's assets in: ‣ Traditional bankruptcy proceedings ‣ Pre-pack liquidation ‣ Remedial proceedings under Art. 323 of the Restructuring Law

Cross-class cramdown mechanism

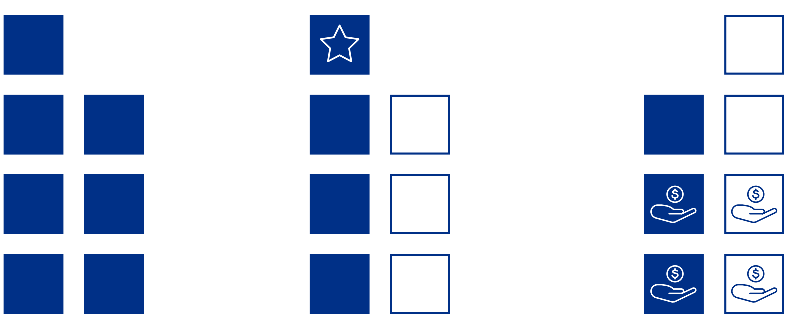
The bill also provides for transposition of a new mechanism for approving an arrangement against the opposition of a group of creditors, known as the cross-class cramdown, as provided for in Art. 11 of Directive 2019/1023.

In principle, to conclude an arrangement in restructuring proceedings, the required majority of votes must be obtained in each creditor class. The essence of the new cross-class cramdown mechanism is that in the absence of the majority needed to approve the arrangement in each creditor class, the arrangement will be approved at the debtor's request or with the debtor's consent if a majority of the creditor classes voted in favour of the arrangement, including at least one group of secured creditors or creditors with a higher degree of priority than category II under the Bankruptcy Law. If this condition is not met, the arrangement may also be approved if a class or classes of creditors representing at least half of the classes belonging to those categories of creditors that would have received any satisfaction in the event of bankruptcy proceedings, using a valuation assuming the continuation of the debtor's business, voted in favour of the arrangement.

To put it simply, the creditors who would have priority in bankruptcy proceedings and creditors who would obtain at least partial satisfaction in bankruptcy proceedings will have greater "voting power."

In the arrangement, the possibility of differentiating the legal position of creditors who would be equally favoured in bankruptcy is also to be limited. The court could not approve the arrangement if the degree of satisfaction of the group of creditors who oppose the arrangement would be less under the arrangement than if bankruptcy proceedings were underway.

WHEN WILL AN ARRANGEMENT BE APPROVED?



In every class of creditors, the required majority of voting creditors voted for the arrangement

A majority of creditor classes voted for the arrangement, including at least one privileged category

At least half of the classes that would receive at least partial satisfaction in a bankruptcy proceeding voted for the arrangement

Date of entry into force of new solutions

The bill is currently at the consultation stage. Taking into account the 18-month grace period provided for in the bill, implementation of Directive 2019/1023 in Poland will most likely take place sometime in 2024.

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